



CITY OF LODI COUNCIL COMMUNICATION

AGENDA TITLE: Adopt Resolution to approve Program Guidelines of the Revolving Loan Fund for the City of Lodi's Economic Development Jobs Program.

MEETING DATE: September 20, 2006

PREPARED BY: Community Improvement Manager

RECOMMENDED ACTION: Adopt Resolution approving the Program Guidelines for the Revolving Loan Program which is the key element of the Community Development Block Grant (CDBG) funded Economic Development Jobs Program.

BACKGROUND INFORMATION: In Council action on March 1, 2006, \$150,000 in CDBG funds were allocated to facilitate the start up of an Economic Development Jobs Program.

Prior to that, at the Shirtsleeve Meeting on February 28, 2006, a presentation was made by Community Development Department (CDD) staff and Carleen Bedwell, Managing Principal with Applied Development Economics, to introduce Council to the concept of the use of CDBG funds for economic development, specifically for the creation of jobs within the community. On July 18, 2006, a draft of the program guidelines, business loan application and the review of the various stages of the loan process was previewed to the Council in a Shirtsleeve Session.

Since that time, Ms. Bedwell has continued to work with CDD staff, with a representative of the County's Revolving Loan Fund Program and with our County CDBG Program Administrator to fine tune the details of the program's guidelines and processes. The culmination of that work is what we have for presentation at this time in the finalized program guidelines for review and approval. We are also providing sample documents from the Revolving Loan Program and letters of intent from both Farmers and Merchants Bank and the San Joaquin County Revolving Loan Program, whose participation will be outlined later in the communication.

What follows is an overview of the key elements of the Revolving Loan Fund (RLF) Program Guidelines.

Purpose and Source of Funding

The purpose of this program is to provide appropriate financial assistance to businesses located in or moving to Lodi, which in turn create full time jobs while increasing the overall economic base of the community. Funding for this program is provided through an allocation of CDBG funds, initially from the 2006-07 Program Year and proposed allocations of CDBG funds in future Program years, and from the repayment of principal and interest from existing loans. As a revolving loan program, any program income from the repayment of loans made from these initial CDBG allocations, is intended to be "recycled" or loaned again through the same program, much like our CDBG and HOME-funded Housing Assistance Programs have been operated.

APPROVED:

A handwritten signature in dark ink, appearing to read "Blair King", written over a horizontal line.

Blair King, City Manager

Guidelines and Features

There is no minimum or maximum RLF loan amount. Borrowers must, however create at least one full time equivalent job for each \$35,000, or fraction thereof, they receive in RLF assistance. In addition, the overall goal is to leverage at least three private dollars from equity and/or debt for every RLF dollar loaned. On a case-by-case basis with projects involving large job creation, this leverage requirement may be relaxed. Owner equity can be cash and/or land. Land will only be counted for construction projects.

Loan terms shall not exceed seven (7) years and the interest rate is set based on the business needs and financial gap of each loan. If the financial gap is the availability of capital, the interest rate shall be near market rates for the asset being financed. If the financial gap is the cost of capital (rate, term or collateral requirements), then the interest rate is set by evaluating the businesses financial condition to determine at what interest rate the proposed project and job creation become viable.

The fees for loan processing range from .5 percent (.5%) to three percent (3%) of the loan amount requested, depending upon the specifics of the loan. The applicant must pay for any special services required for the loan analysis, such as title search, special environmental studies, and appraisals.

There shall be no prepayment penalty and deferral of payments will be considered on a case-by-case basis.

Job creation is the primary benefit that this program brings to the community. To assist with the job creation to benefit Targeted Income Group persons, the business will be required to sign a First Source Hiring Agreement, which commits the borrower to use the services of WorkNet, the San Joaquin County job training program, as the first source from which to hire new employees. WorkNet is accustomed to assisting employers to find workers within its clientele, and has an office in Lodi. Referrals from WorkNet will have undergone the income verification process which documents their Targeted Income Group status.

In the event the business does not hire from WorkNet, the City's Program Operator will conduct the income verification of job applicants. At least 51% of the jobs created as a result of the loan funds must be filled by persons from the Targeted Income Group.

All loans are to be fully secured for 100% collateral coverage to maintain the RLF Program and no unsecured loans shall be made.

General Credit Requirements

The following general credit criteria will be applied by the RLF.

- Demonstrate the ability to operate the same type of business successfully for 3 years, or document the contracted expertise necessary to offset deficiencies in the principal's background or training.
- If circumstances warrant, agree to attend Small Business Development Center business plan, financial and marketing courses. Have enough financial strength and borrowing ability or equity to operate with the RLF assistance, on a sound financial basis.
- Show that the proposed assistance is reasonably secured to assure repayment.
- Show that the past earning record and future prospects of the business indicate ability to repay the loan and other fixed debt, if any, from the operation of the business.

Eligibility

Eligible applicants include on-going private, for profit business concerns, corporations, partnerships, and sole proprietorships that are classified as industrial, commercial or retail businesses, and that are located in or expanding to the City of Lodi.

Eligible costs within the RLF are as follows:

- Infrastructure and off-site improvements.
- Land costs, including engineering, legal, grading, testing, site mapping and related costs associated with the acquisition and preparation of land.
- Building construction costs, including real estate, engineering, architectural, legal and related costs associated with acquisition, construction and rehabilitation of buildings and tenant improvements. It is important to note that the use of loan funds in private construction triggers federal Labor Standards and requires the payment of Prevailing Wage. In addition, the use of loan funds for any of the eligible costs may trigger state Prevailing Wage.
- Purchase of inventory, furniture, fixtures, machinery and equipment.
- Impact/Mitigation fees.

Ineligible costs within the RLF are as follows:

- Projects which do not meet the purpose of the program are not eligible.
- Costs incurred prior to CDBG grant execution, or prior to submittal of the loan application, and prior to environmental review completion are ineligible, except for private expenditures specifically identified in the application.
- Projects, which are not located in the City of Lodi.
- Projects which involve the relocation of residents or businesses.
- Projects that propose the refinancing of existing debt are not eligible.
- Projects are not eligible if they create a conflict of interest pursuant to California Government Code Section 87100 et seq. for any current City elected official, appointed official, or employee.

The Revolving Loan Fund Program will be operated through a combination of public and private services. The City retains the option to modify these service providers, once the program has gotten underway and the City has experience with it. The City of Lodi will, through the City Manager's Office and the Community Development Department, maintain the following rights and duties in administration of the RLF Program:

- Oversight of the program
- Agreements for service with County Business RLF, and Farmers & Merchants Bank, and/or other future service providers.
- Selects local banking and business professionals that are recommended by the Mayor and Council to sit on the Loan Advisory Committee.
- Marketing and initial screening of potential applicants.
- Attends Loan Advisory Committee meeting for each loan presentation.
- Annual reporting to San Joaquin County CDBG program on status of business loans, jobs created, and use of CDBG funds.
- Approval or denial of individual loans recommended by Loan Advisory Board.
- Legal review of documents
- Execution of loan documents
- Release of funds.
- Collection process
- Liaison responsibility with County CDBG program and service providers.

Due to their extensive knowledge and experience in operating this type of program using federal funding, the San Joaquin County Revolving Loan Fund Office will act as the City's Program Operator and will have the following responsibilities for operating the RLF Program:

- Assist the business applicant with application process in the Second Phase of the application process.
- Conduct loan underwriting, using HUD underwriting guidelines.
- Prepare Credit Memo for Loan Advisory Committee (LAC) and present to LAC.
- Transmit the LAC action to the City Manager, with draft approval letter.
- Once loan has been made, provide loan servicing.
- Collect annual job and financial reporting from borrowers, and submit annual loan program activity report to City.
- Provide income verification process to certify Targeted Income Group benefiting from created jobs.

Farmers and Merchants Bank of Lodi has agreed to provide the following service in support of the RLF Program:

- Obtain software to be used for City loan program documents.
- Prepare loan documents for each loan.
- Conduct loan closing on each loan.

Review of RLF Process

What follows is an initial overview of the entire loan review process, followed by a brief summary of each step in the process.

- Loan Application Review/Approval Process
 - Qualitative Review by City Manager, Assistant City Manager & Community Development Director
- Program Operator Review Process
 - Collection of quantitative data, documents.
 - Credit analysis and loan underwriting process.
 - Compliance with adopted Program Guidelines and Federal Housing and Urban Development (HUD) Guidelines for underwriting.
 - Recommendation to Loan Advisory Committee.
- Loan Advisory Committee Review
 - Committee of 3-5 persons with banking and business background, recommended by the Mayor and City Council, and selected by City Manager.
 - Reviews Credit Memo from Program Operator.
 - Makes formal recommendation to City Manager including terms and conditions of the loan.
- City Manager Review and Approval
 - Final decision on approval or denial.
- Loan Documents and Closing
 - Approved loans are forwarded for preparation of loan documents.
 - Bank performs closing with oversight by City Staff.
- Loan Servicing
 - Monitoring for compliance with conditions and HUD Guidelines.
 - Verifying job creation compliance.
 - Payment processing, reporting and collection of delinquent accounts.

Loan Application Review/Approval Process

Based upon information provided by the potential applicant, a committee of City staff will review the project for loan application appropriateness and eligibility. The Committee will be composed of the City Manager, Deputy City Manager, and Community Development Director. No fee will be charged for this phase.

In the event the potential project has been determined to be an eligible project and appropriate for CDBG loan consideration, the applicant will complete a Lodi Revolving Loan Fund Application.

Program Operator Review Process

In the Second Phase of the loan application process, the City's Program Operator will act as the City's representative and primary contact as the loan applicant compiles all necessary loan application documents. The Program Operator will conduct the loan underwriting process, using HUD Underwriting Guidelines, which are attached to these Guidelines. City staff will provide oversight to the program and all aspects of it.

As a result of the loan underwriting process, a Credit Memo will be prepared with an analysis of the loan and the recommended action to be taken. If a loan is recommended for approval, the Credit Memo will contain the loan structure, including terms and conditions. The Credit Memo will be sent to the Loan Advisory Committee.

Loan Advisory Committee Review

A Loan Advisory Committee (LAC) shall be composed of 3-5 persons from a list of local banking and business professionals that have been recommended by the Mayor and City Councilmembers. The City Manager wishes to maintain a pool of approximately 8-10 candidates from which to draw upon to serve on the LAC on a case by case basis. In addition to providing the aforementioned loan documentation services, Farmers and Merchants Bank has also offered to provide a representative to serve on the LAC.

The LAC is responsible for reviewing loan applications as forwarded through the Credit Memo provided by the City's Program Operator, the County RLF Program. The recommendations of the Loan Advisory Committee are made in writing to the City Manager.

City Manager Review and Approval

The City Manager will make the final decision on approval or denial of all loan applications submitted, including terms and conditions of loan agreements.

Loan Documents and Closing

Once the loan is approved, final loan documents will be prepared by the Farmers & Merchants Bank. The bank, acting as the city's representative, will conduct the loan closing, with oversight by City staff.

Loan Servicing – Monitoring

The San Joaquin County RLF Program, as our Program Operator, will have the responsibility for loan servicing functions, including payment processing, reporting and collection of delinquent accounts. At this point, the County RLF Program has agreed to provide these services pro bono for the first loan, until the appropriate costs are determined.

The Program Guidelines include the following attachments:

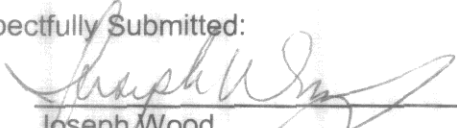
Attachment A Target Income Group Income Levels
Attachment B Loan Underwriting Guidelines

The following program documents are provided as attachments to this Council Communication:

Exhibit A Program Guidelines and Attachments A & B
Exhibit B Sample RLF Loan Application
Exhibit C Sample Commitment Letter
Exhibit D Sample Credit Memo
Exhibit E Sample Loan Agreement and Covenants and Conditions
Exhibit F Letter of Intent from San Joaquin County RLF Program Office
Exhibit G Letter of Intent from Farmers & Merchants Bank

FUNDING: 2006/07 CDBG Allocation \$150,000

Respectfully Submitted:



Joseph Wood
Community Improvement Manager

Concurred:



Randy Hatch
Community Development Director

Attachments

CITY OF LODI REVOLVING BUSINESS LOAN FUND

PROGRAM GUIDELINES

PURPOSE

The City of Lodi Revolving Loan Fund (RLF) is designed to meet the capital needs of businesses located in or moving to the City of Lodi. An RLF, in this context, refers to a loan program in which loan repayments are “revolved” or “recycled” to be loaned again in the same program

The RLF will provide appropriate assistance to businesses, which in turn create full time jobs while increasing the overall economic base of the community.

- The RLF is designed to provide no more than one-quarter of a project’s total financing requirements.
- The RLF will only provide the funds necessary to bridge the financial gap that allows the project to move forward.
- The RLF is targeted to businesses that have the greatest potential for long-term job creation, primarily benefiting persons in the Targeted Income Group¹(TIG) – which is a national objective of the HUD CDBG program. In addition, priority will be given to projects with other local public benefits, such as contribution to the City’s tax base, and local investment.

SOURCE OF FUNDING

The source of the funding for the RLF is the Community Development Block Grant Program (CDBG) of the federal Department of Housing & Urban Development (HUD) through the County of San Joaquin, and the repayment of principal and interest from existing loans. Federal requirements are incorporated into the use of these funds.

GUIDELINES AND FEATURES

There is no minimum or maximum RLF loan amount. Borrowers must, however create at least one full time equivalent job for each \$35,000, or fraction thereof, they receive in RLF assistance.

The following guidelines have been adopted to clarify the program basis for making loan commitment decisions.

- **Leveraging:** The RLF Program’s overall goal is to leverage at least three private dollars from equity and/or debt for every RLF dollar loaned. On a case-by-case basis with projects involving large job creation, this leverage requirement may be relaxed. Owner equity can be cash and/or land. Land will only be counted for construction projects. Expenditures made by the loan applicant prior to the RLF loan award are not counted unless made as part of the submittal, and made within 60 days of the application

¹ A household whose annual income is less than 80% of the county median income as defined by the County of San Joaquin CDBG Program. The income amounts change annually. See Attachment A for 2006 income levels.

submittal to the RLF, and are related to and in anticipation of RLF funding. If the equity requirement is relaxed for a project, additional collateral will be required.

- **Loan Terms:** Not to exceed seven (7) years depending on the asset being financed, the financial gap, and the demonstrated need for the RLF funds. This is subject to participating lender criteria and the quality of collateral. A call provision prior to the loan maturity date may be incorporated.
- **Interest Rate:** The interest rate is set based on the business needs and financial gap of each loan. If the financial gap is the availability of capital, the interest rate shall be near market rates for the asset being financed. If the financial gap is the cost of capital (rate, term or collateral requirements), then the interest rate is set by evaluating the businesses financial condition to determine at what interest rate the proposed project and job creation become viable.
- **Loan Fees:** There is no fee charged for the Phase 1 of the loan application process, the Initial Phase. The fees for loan processing in the Second Phase range from .5 percent (.5%) to three percent (3%) of the loan amount requested, depending upon the specifics of the loan. The applicant must pay for any special services required for the loan analysis, such as title search special environmental studies, and appraisals.
- **Prepayment Penalty:** None
- **Deferral Payments:** On a case-by-case basis, payments may be deferred if warranted by the financial needs of the business.
- **Job Creation:** At least one full time equivalent job (1,750 hours annually) per \$35,000 provided (or fraction thereof) must be achieved for each business assisted. Two permanent part-time jobs (at least 875 hours annually) can be aggregated to count as one full time equivalent job in the same project. At least 51% of all jobs created/retained shall be held by Targeted Income Group (TIG) persons. See Attachment “A” for Current Income Limits of Targeted Income Group.
- **Collateral Requirements:** All RLF loans are to be fully secured for 100% collateral coverage to maintain the RLF Program. No unsecured loans shall be made. Types of collateral may include one or more of the following:
 - Real Estate – liens on real property supported by appraisals establishing sufficient equity generally utilizing a 100% loan to value ratio.
 - Deeds of Trust.
 - Liens on RLF financed machinery, equipment, or other fixtures, generally a 95% loan to value ratio.
 - Assignment of Rents, as appropriate.
 - Personal and/or Corporate Guarantees, as appropriate.
 - Cosigners and other collateral such as insurance on principals.
 - Other collateral, as appropriate.

GENERAL ADMINISTRATIVE FEATURES

- NEPA Environmental Review of business project.
- Equal Opportunity/Affirmative Action Policy.
- Attorney review of all contracts and legal forms.
- Monitoring and reporting forms.
- Collection and foreclosure policy.
- Compliance with HUD program regulations.

- Federal and State Labor Standards where applicable.

GENERAL CREDIT REQUIREMENTS

The following general credit criteria will be applied by the RLF. These requirements must be satisfied in conjunction with the provisions of RLF assistance so that the assistance is not allowed to compensate for deficiencies in these criteria. An Applicant must:

- Demonstrate the ability to operate the same type of business successfully for 3 years, or document the contracted expertise necessary to offset deficiencies in the principal's background or training.
- If circumstances warrant, agree to attend Small Business Development Center business plan, financial and marketing courses. Have enough financial strength and borrowing ability or equity to operate with the RLF assistance, on a sound financial basis.
- Show that the proposed assistance is reasonably secured to assure repayment.
- Show that the past earning record and future prospects of the business indicate ability to repay the loan and other fixed debt, if any, from the operation of the business.

ELIGIBLE APPLICANTS

Eligible applicants include on-going private, for profit business concerns, corporations, partnerships, and sole proprietorships that are classified as industrial, commercial or retail businesses, and that are located in or expanding to the City of Lodi. The project to be financed with the RLF Program must be within the incorporated area of the City of Lodi.

ELIGIBLE COSTS

- Infrastructure and off-site improvements.
- Land costs, including engineering, legal, grading, testing, site mapping and related costs associated with the acquisition and preparation of land.
- Building construction costs, including real estate, engineering, architectural, legal and related costs associated with acquisition, construction and rehabilitation of buildings and tenant improvements. (See note below regarding Labor Standards and Prevailing Wage.)
- Purchase of inventory, furniture, fixtures, machinery and equipment.
- Impact/Mitigation fees.

Special Note

The use of loan funds in private construction triggers federal Labor Standards and requires the payment of Prevailing Wage. In addition, the use of loan funds for any of the eligible costs may trigger state Prevailing Wage. This is determined on a case by case basis, and should be discussed with loan staff as early in the process as possible.

INELIGIBLE USES

- Projects which do not meet the purpose of the program are not eligible.
- Costs incurred prior to CDBG grant execution, or prior to submittal of the loan application, and prior to environmental review completion are ineligible, except for private expenditures specifically identified in the application.
- Projects, which are not located in the City of Lodi.
- Projects which involve the relocation of residents or businesses.

- Projects that propose the refinancing of existing debt are not eligible.
- Projects are not eligible if they create a conflict of interest pursuant to California Government Code Section 87100 et seq. for any current City elected official, appointed official, or employee.

OPERATION OF THE PROGRAM

The City of Lodi Business Revolving Loan Program will be operated through a combination of public and private services. The City retains the option to modify these service providers, once the program has gotten underway and the City has experience with it.

City of Lodi

- Oversight of the program
- Agreements for service with County Business RLF, and Farmers & Merchants Bank, and/or other future service providers.
- Appoints the Loan Advisory Committee.
- Marketing and initial screening of potential applicants.
- Attends Loan Advisory Committee meeting for each loan presentation.
- Annual reporting to San Joaquin County CDBG program on status of business loans, jobs created, and use of CDBG funds.
- Approval or denial of individual loans recommended by Loan Advisory Board.
- Legal review of documents
- Execution of loan documents
- Release of funds.
- Collection process
- Liaison responsibility with County CDBG program and service providers.

City's Program Operator, San Joaquin County Revolving Loan Fund

- Assist the business applicant with application process in the Second Phase of the application process.
- Conduct loan underwriting, using HUD underwriting guidelines.
- Prepare Credit Memo for Loan Advisory Committee (LAC) and present to LAC.
- Transmit the LAC action to the City Manager, with draft approval letter.
- Once loan has been made, provide loan servicing.
- Collect annual job and financial reporting from borrowers, and submit annual loan program activity report to City.
- Provide income verification process to certify Targeted Income Group benefiting from created jobs.

Farmers & Merchants Bank

- Obtain software to be used for City loan program documents.
- Prepare loan documents for each loan.
- Conduct loan closing on each loan.

LOAN APPLICATION

Initial Phase

Based upon information provided by the potential applicant, a committee of City staff will review the project for loan application appropriateness and eligibility. The Committee will be composed of the City Manager, Deputy City Manager, and Community Development Director. No fee will be charged for this phase.

Information to be provided by the potential applicant includes:

- Description of the business and project,
- Amount of loan funds requested,
- Number of jobs to be created and potential for TIG benefit
- Other public benefits
- Intended use of the funds
- Project timing and job creation timing
- Leverage and status of funding
- Environmental considerations
- Principals of the business and business plan.

Second Phase

In the event the potential project has been determined to be an eligible project and appropriate for CDBG loan consideration, the applicant will complete a Lodi Revolving Loan Fund Application.

In the Second Phase of the loan application process, the County Business Loan Program will act as the City's representative and primary contact as the loan applicant compiles all necessary loan application documents. The County Business Loan Program will conduct the loan underwriting process, using HUD Underwriting Guidelines, which are attached to these Guidelines. City staff will provide oversight to the program and all aspects of it.

As a result of the loan underwriting process, a Credit Memo will be prepared with an analysis of the loan and the recommended action to be taken. If a loan is recommended for approval, the Credit Memo will contain the loan structure, including terms and conditions. The Credit Memo will be sent to the Loan Advisory Committee.

LOAN REVIEW

The Loan Advisory Committee (LAC) is responsible for reviewing loan applications as forwarded through the Credit Memo provided by the City's Program Operator, the County RLF Program. The recommendations of the Loan Advisory Committee are made in writing to the City Manager. The City Manager will make the final decision on approval or denial of all loan applications submitted, including terms and conditions of loan agreements. All projects moving forward from the Initial Screening Phase and completed Loan Applications will be brought before the LAC.

The Loan Advisory Committee shall be composed of 3-5 persons and appointed by the City Manager. The appointments will be persons with business and/or banking experience.

On average, the RLF review process takes six to eight weeks from submittal of a complete loan application through Loan Advisory Committee review. Every effort will be made to facilitate the process to coincide with the other funding sources and the project's requirements.

LOAN CLOSING

Once the loan is approved, final loan documents will be prepared by the Farmers & Merchants Bank. The bank, acting as the city's representative, will conduct the loan closing, with oversight by City staff.

LINKING JOBS WITH TARGETED INCOME GROUP PERSONS

To assist with the job creation to benefit Targeted Income Group persons, the business will be required to sign a First Source Hiring Agreement, which commits the borrower to use the services of WorkNet, the San Joaquin County job training program, as the first source from which to hire new employees. WorkNet is accustomed to assisting employers to find workers within its clientele, and has an office in Lodi. Referrals from WorkNet will have undergone the income verification process which documents their Targeted Income Group status.

In the event the business does not hire from Worknet, the City's Program Operator, the County Business RLF, will conduct the income verification of job applicants. At least 51% of the jobs created as a result of the loan funds must be filled by persons from the Targeted Income Group.

IF JOBS NOT CREATED

In the event the business does not create the jobs as specified in the Loan Agreement and related documents, the City will declare the loan in default and require full repayment.

HOW TO GET STARTED

Please take time to read and understand the information outlined above. If you are interested in learning more about the program, please contact:

Joseph Wood
Community Improvement Manager
City of Lodi
221 West Pine Street, P. O. Box 3006
Lodi, California 95241-1910
Phone: (209) 333-6823
jwood@lodi.gov

ATTACHMENT A
CURRENT TARGET INCOME GROUP INCOME LEVELS

Percent of Median Income				
Family Size	Very-Low			Low
	0-30%	31-50%	51-60%	61-80%
1	11,986	19,977	23,972	31,963
2	13,709	22,848	27,417	36,556
3	15,431	25,719	30,862	41,150
4	17,130	28,550	34,260	45,680
5	18,499	30,831	36,997	49,330
6	19,890	33,151	39,781	53,041
7	21,259	35,432	42,518	56,691
8	22,628	37,713	45,256	60,341
9	23,965	39,941	47,930	63,906
10	25,352	42,254	50,705	67,606
11	26,723	44,538	53,446	71,261
12	28,093	46,822	56,186	74,915
13	29,464	49,106	58,927	78,570

Note: These figures change annually, and are provided by the San Joaquin County CDBG Program.

ATTACHMENT B

LOAN UNDERWRITING GUIDELINES

The loan underwriting policies of the City of Lodi RLF are designed to assist businesses that could not proceed without the RLF assistance and to ensure that the RLF assistance is “appropriate” as defined by HUD.

HUD UNDERWRITING GUIDELINES

The City of Lodi has adopted the HUD underwriting guidelines to determine whether a proposed RLF subsidy is *appropriate* to assist the business expansion or retention. In addition, the project will be reviewed to determine that a minimum level of *public benefit* will be obtained from the expenditure of the CDBG funds.

The objectives of the underwriting guidelines are to ensure that:

Project costs are reasonable.

All sources of project financing are committed.

RLF funds are not substituted for non-Federal financial support.

The project is financially feasible.

The return on the owner’s equity investment will not be unreasonably high.

RLF funds are disbursed on a pro rata basis with other financing provided to the project.

Sufficient public benefit will be received from the expenditure of RLF funds.

Project Costs: All project costs will be reviewed for reasonableness, and to avoid providing either too much or too little RLF assistance. The amount of time and resources expended evaluating the reasonableness of a cost element shall be commensurate with its costs. In some instances, it will be necessary to obtain third-party fair-market price quotations or a cost estimate. Particular attention will be focused on documenting the cost elements in a non-arm’s length transaction.

Commitment of All Sources of Project Financing: Prior to the commitment of RLF funds to the project, a review shall be conducted to determine if sufficient sources of funds have been identified and committed to the project, the Borrower and participating lenders have the financial capacity to provide the funds, and to ascertain if the project is viable and will move ahead in a timely manner. In certain circumstances, the RLF may commit its funds in advance of final commitments from other funding sources. However, to conduct the underwriting analysis, the approximate terms and conditions of the other funding sources should be known. Final commitments from the other funding sources will be required, with substantially similar terms and conditions as used in the underlying analysis, prior to any loan closing or disbursement of funds.

Avoid Substitution of RLF Funds for Non-RLF Financial Support: The project will be reviewed to ensure that, to the extent practicable, RLF funds will not be used to substantially reduce the amount of non-RLF financial support for the project.

In order to receive RLF funds, a project must have a “financial gap.” This gap must be documented. There are three types of financial gaps, two are discussed below, and the third is discussed under the criterion “Return on Equity Investment.” One project may have two different gaps. The types of gaps are as follows:

Unavailability of Capital: The project can afford the cost of financing, but is unable to obtain the funds from either debt and/or equity sources. In regard to debt, the gap may be a result of a lender’s loan to value requirements or the inherent risk of the industry or project. For example, the lender will only loan 70% of the project’s cost. In this case, the business may not have the cash to bridge the gap, or if the business bridges the gap, its cash flow may be so restricted as to jeopardize the business. In order to document this gap, several steps need to be undertaken. The lender needs to be contacted to determine if there is any ability to increase the size of their loan. Other lending sources, both public and private, need to be explored. This includes looking at the business owner(s) personal financial statements for potential funds, including home equity loans. Finally, in addition to looking at the business and personal financial statements and tax returns, a proforma cash flow analysis needs to be prepared and analyzed, with and without RLF funds, to demonstrate the gap. The terms and conditions of a loan under this gap analysis should be comparable to the market.

Cost of Capital: The project cannot support the interest rate, loan term and/or collateral requirements of a lender. In analyzing this gap, discussions with the lender are important to determine any flexibility in terms. A single project may not be able to support the rate, terms and collateral requirements, or may just face a single hurdle. In addition, the gap may only exist in the early years of the project. To determine the gap, business and personal financial statements and tax returns shall be analyzed. Sources of equity shall be explored. Public and private funding sources that would bridge the gap shall be evaluated. Proforma cash flow analysis shall be developed with and without the RLF funds to demonstrate the gap. Depending on the gap, the terms or rate shall be adjusted to a rate that allows the project to proceed but are not too generous. Terms can be adjusted to allow for deferrals of principal and or interest, or to allow loans to be amortized over a longer period. Interest rates can be adjusted, including increases in the rate over time as cash flow allows.

Financial Feasibility of the Project: Each project will be examined to determine the financial viability of the project, and thus the reasonable assurance that the public benefit will be realized. The current and past financial statements for both the business and individuals must be analyzed, along with tax returns and projections. The assumptions behind the projections must be critically analyzed. Income and expense costs shall be evaluated and compared historically, where applicable, and compared to industry averages (using guides such as Robert Morris Annual Financial Statements). Project costs, including both hard and soft costs, must be determined to be reasonable. Accurate project costs are vital to determining project feasibility. As part of the financial analysis, the past, current, and projected financial data shall be analyzed to determine if the job estimates are reasonable and supportable. Labor costs shall be gauged at the break-even

point. In addition, labor costs shall be checked against industry averages. Any variations shall be explained in the loan analysis.

The terms and conditions of the RLF loan must be “appropriate.” In general, the interest rate shall be set at a rate where available cash flow is able to meet debt obligations, after other obligations are met, with enough cash flow remaining to operate successfully. The loan term typically is based on the asset being financed. The term should not exceed the economic life of the asset being financed. However a longer loan amortization schedule, with the loan due at the end of the economic life may be justifiable.

Each loan shall include a written explanation of the “appropriate” analysis that was undertaken, and the reason the terms and conditions of the loan were approved. Each loan decision shall also contain a certification statement by the City Manager that the loan has been reviewed according to all underwriting guidelines and regulations and that the loan is appropriate by state/federal definition.

Financial Analysis: Historical and projected financial statements will be subject to financial analysis to determine the gap, and structure the terms and conditions of the RLF loan, as discussed above, but also to determine that the project is feasible. In addition, using prudent underwriting guidelines, demonstrate that the proposed loan is of sound value and that past earnings and future prospects indicate an ability to meet debt obligations out of profit.

Information required to be submitted by the applicant will depend on the project, ownership structure and whether it is an ongoing or start-up business. In general, the information required is outlined in the RLF checklist that will be provided.

The financial analysis will be designed to evaluate the business. The analysis will include a spread of the current and past financial statements to determine trends. The proforma statements will then be compared to these statements. Key financial ratios will be analyzed. The statements and key ratios will be compared to industry averages. Key ratios that will be analyzed include:

Current Ratio: current assets/current liabilities. The ratio is a rough indication of a firm’s ability to service its current obligations. A ratio of 2:1 will be considered secure.

Quick Ratio: cash and equivalents plus accounts & notes receivable/current liabilities. This ratio is a refinement of the current ratio. A ratio of 1:1 will be used to demonstrate ample liquidity.

Cash Flow Coverage: net profit and depreciation and depletion-amortization expenses/current portion of long-term debt. This ratio will be used to measure the ability to service long term debt. This ratio is a measure of a firm’s ability to meet interest payments. A cash flow coverage of 1.25 times debt service shall be used as a guideline.

Debt to Worth: total liabilities/tangible net worth. This ratio is the relationship between debt and a businesses net worth. A lower ratio is an indication of greater long-term financial safety and greater flexibility to borrow. In general, a debt to worth ratio of

higher than 5:1 shall not be exceeded as an underwriting policy. There are exceptions when the industry average is high due to its capital intensive nature or when projections show the ratio lowering quickly.

Collateral Coverage: The value of collateral is compared to the amount of the loan. Typical underwriting guidelines suggest that 125% of loan balance be used. This ratio is highly dependent on the quality and security of the collateral. The Lodi RLF shall use 100% as a guideline, which shall only be lowered with specific and detailed analysis and explanation.

Break-even Analysis: The analysis of the project's ability to support the projected labor costs and additional debt service at its break-even point (BEP) will be analyzed to determine what proportion of the jobs can be supported at that BEP. This will serve as a worst case look at the business prospects for success, ability to service new debt, and meet job creation/retention obligations.

The financial and ratio analyses must be supported by the business plan. The business plan must provide a clear understanding of the project, competition, market strategy, sales estimates, management capacity and other factors.

Lastly, to ensure project feasibility, an evaluation will be conducted of the experience and capacity of the business principals to manage the business and achieve the projections.

Return on Equity Investment: The return on equity investment is the amount of cash that the investor/business owner is projected to receive in relation to their initial equity. For a sole proprietor, this equates to salary plus net income. The RLF should not provide more than a reasonable return on investment to the business owner. This will help ensure that the RLF will maximize the use of RLF funds and not unduly enrich the business owner(s)/investor(s). However care shall be taken to ensure that the rate of return will not be too low so that the business owner's motivation remains high to pursue the business with vigor.

If the project's financial returns are projected to be too low to motivate the business and/or investor to proceed with the project, the risks of the project may outweigh the returns. An inadequate rate of return adjusted for industry and locational risks, is a third method used to determine the gap appropriate to be funded with RLF funds. To analyze this gap, the projected return on investment must be compared to the return on investment on similar projects. If it is shown that a gap does exist then the RLF financing rate and terms must be set at a rate which provides a return equal to the "market rate." Real estate appraisers and lenders will be used as sources of information on "market rate" returns.

Disbursement of RLF Funds on a Pro Rata Basis: To the extent practicable, RLF funds should be disbursed on a pro rata basis with other funding sources to avoid placing RLF funds at a greater risk than other funding sources. When it is determined that it is not practicable to disburse RLF funds on a pro rata basis, other steps shall be taken to safeguard RLF funds in the event of a default.

Standards for Evaluating Public Benefit: Each project will be reviewed to determine if a minimum level of public benefit will be obtained from the expenditure of RLF funds. The minimum standards are:

- Project site within the incorporated boundaries of the City of Lodi.
 - The project must lead to the creation or retention of at least one full-time equivalent job per \$35,000 or fraction thereof of RLF funds borrowed.
 - The timing of job creation must be reasonable in relation to the receipt of RLF assistance.
-
-

CITY OF LODI REVOLVING LOAN FUND (RLF)**LOAN APPLICATION****I. COMPANY INFORMATION**

Name: _____

Address: _____

Telephone Number: _____

Contact Person: _____

Project Address: _____

Project Assessor Parcel Number(s): _____

Current yearly property taxes: _____

Business legal structure: _____ Proprietorship

_____ Partnership

_____ Corporation

Years in business: _____

Current number of employees: Full time: _____

Part time: _____

Projected number of employees after completion of project:

Full time: _____

Part time: _____

Number of employees to be hired during year one: _____

Number of employees to be hired during year two: _____

Total number of new employees: _____

Total number of employees two years from completion of project: _____

111. PRINCIPAL(S) INFORMATION

Name: _____

Position: _____

% of ownership: _____

Years of experience: _____

Name: _____

Position: _____

% of ownership: _____

Years of experience: _____

III. EXISTING FACILITY

Size: _____ square feet

Owned or leased: _____

If owned:

Purchase price \$ _____

Existing mortgage \$ _____

Recent appraised value \$ _____

Annual mortgage payments \$ _____

If rented:

Monthly rent \$ _____

Annual rent \$ _____

Expiration date of lease _____

IV. NEW/EXPANDED INFORMATION (IF APPLICABLE)

Size after expansion: _____ square feet

Will new facility replace existing facility? _____

If replaced, will rent be saved or will existing facility be sold? _____

For how much can existing facility be sold? \$ _____

Purchase price of new facility \$ _____

Appraised value \$ _____

Lease rate of new facility \$ _____

Lease term _____

Will purchaser/lessee occupy entire space? _____

If no, explain other uses: _____

% to be occupied by purchaser: _____

Rental income generated: \$ _____

V. PRINCIPAL BANK INFORMATION

Name of bank: _____

Contact person: _____

Telephone number: _____

Available line of credit: _____

VI. PROJECT COSTS

New construction	\$ _____
Rehabilitation	\$ _____
Off site improvements	\$ _____
Acquisition	\$ _____
Equipment	\$ _____
Working capital	\$ _____
Other	\$ _____
TOTAL	\$ _____

VII. PROJECT FUNDING

RLF	\$ _____
Bank	\$ _____
Company	\$ _____
Other	\$ _____
TOTAL	\$ _____

VIII. PROJECT DESCRIPTION (NARRATIVE)

IX. ADDITIONAL INFORMATION

X. INFORMATION REQUESTED FOR LOAN UNDERWRITING

- _____ Business income statements (current and last three years)
- _____ Business balance sheets (current and last three years)
- _____ Business income tax returns (last three years)
- _____ Personal income statements and balance sheets for business owners (current and last three years)
- _____ Individual tax returns for business owners (last three years)
- _____ Company history and resumes of principals
- _____ Copy of articles of incorporation, by-laws, corporation certificate of good standing, fictitious name statement, partnership agreement, or franchise agreement, as applicable.
- _____ Pro forma cash flow statement
- _____ Pro forma balance sheet
- _____ Business plan
- _____ Preliminary title report on property to be used as collateral
- _____ Appraisal of property to be used as collateral
- _____ Schedule of business debt and summary of lease payments on equipment and building
- _____ Sources and uses of funds (e.g., equipment list, project cost estimates)
- _____ Bank letter of commitment, as applicable
- _____ Copy of purchase agreement or lease agreement, as applicable

I/we hereby acknowledge that the City of Lodi does not and cannot guarantee that I/we will receive financing from the RLF or from public or private lenders. In addition, RLF financing will not be provided without adequate documentation regarding funding of the balance of project costs. By my/our signature below, I/we grant permission to conduct necessary reviews of my/our financial and credit histories. I/we understand job creation is a requirement of the loan.

APPLICANT SIGNATURE: _____
PRINTED NAME: _____ DATE: _____

APPLICANT SIGNATURE: _____
PRINTED NAME: _____ DATE: _____

CITY OF LODI REVOLVING LOAN FUND (RLF)

NEPA REVIEW REQUEST FORM

Application Date: _____

Company Name: _____

Project Address: _____

Contact Person: _____

Telephone Number: _____

Concise description of proposed project:

Approximately date application to be presented to Loan Committee: _____

Date NEPA request forwarded to Planning: _____

Planner assigned: _____

Date completed by Planner: _____

XXXXXXXXXXXX XX, 2006

XXXXXXX
XXXXXXX
XXXXXXX
XXXXXXX

Re: Application for Lodi Revolving Loan Fund Financing

Dear XXXXXXX:

I am pleased to inform you that the City of Lodi approves Lodi Revolving Loan Fund (RLF) financing for your business.

You should understand that this approval does not constitute a commitment to lend by the RLF, but that it is a required, as well as an important step in processing your funding request. This letter will summarize the general scope of the proposed loan and is intended for discussion purposes only as an aid in the preparation of final documentation.

This does not constitute a commitment by the RLF to loan and is not a complete statement of all terms, conditions and documents that may be required in connection with this proposed loan.

No lending commitment will exist until final loan documents have been prepared and approved by the City Attorney and executed by all required parties. The loan transaction will then be governed by that final Loan Agreement which will supersede any and all negotiations and discussions of the parties.

TERM SHEET

1. Principal Loan Amount: \$
2. Interest Rate:
3. Loan Term: .
4. Payment:
5. Use of Loan Proceeds:
6. Collateral [Mark as Appropriate]:
 - ☐ a. Machinery & Equipment
 - ☐ b. Inventory
 - ☐ c. Accounts Receivable
 - ☐ d. Residential Real Estate

7. Fees/Costs:

8. Miscellaneous:

A list of covenants and conditions to RLF loans is also attached for your review. This is not intended to be a complete or exhaustive list and is likely to be modified in the final loan documentation.

Please review this letter carefully and, if you desire to proceed with the loan process, sign and return the original and keep a copy for your information. Although this letter does not constitute an agreement to fund you loan, IT DOES REPRESENT YOUR AGREEMENT TO REIMBURSE THE RLF FOR THE COSTS AND LEGAL EXPENSES WHICH IT WILL INCUR IN CONTINUING TO PROCESS THE LOAN. Those costs and legal expenses are estimated on the attached sheet, but you will be required to pay the actual amount of costs and expenses incurred, without reference to the estimates. RLF staff will make its best efforts to notify you if it believes the costs and legal expenses will be in excess of the estimates (but the Borrower releases RLF from any liability for failure to so notify).

If this loan transaction has not closed and/or funded within one hundred twenty (120) days of this letter, the City may deem your loan application withdrawn. We will provide you with a billing for all expenses incurred to that date, which will be immediately due and payable.

If you have not signed and returned this letter to the RLF by xxxxxxxxxxxxxx, the City may deem your application withdrawn.

Should you have any questions regarding this matter, please do not hesitate to contact the RLF office at (209) xxx-xxxxx.

Sincerely,

Blair King
City Manager

Attachments

I have received a copy of this letter, acknowledge its contents and agree to pay the costs and legal fees and expenses referred to herein. I have read, understand and accept all conditions and requirements of this letter.

By: _____

Date: _____

By: _____

Date: _____

SCHEDULE OF FEES AND EXPENSES –REVOLVING LOAN FUND (RLF)

Application Fee: An application fee is due upon staff completion of a preliminary analysis of the loan proposed for submission to the Revolving Loan Fund Board. The fee is as follows:

<u>Loan Application Amount</u>	<u>Application Fee</u>
\$ 10,000.00 to \$100,000.00	\$ 250.00
\$100,001.00 to \$250,000.00	\$ 500.00
\$250,001.00 to an above	\$1,000.00

Upon applicant's review of the terms and conditions of a loan recommendation, should the loan not be recommended and/or approved by the Lodi Loan Advisory Committee and/or the City of Lodi, the loan application fee, or a pro-rated portion thereof, may be refunded to the applicant.

Upon applicant's review and approval of the terms and conditions of a loan recommendation, should the applicant decide to withdraw the loan proposal, the application fee is non-refundable.

Upon loan approval, the loan application fee shall be applied first to legal expenses incurred by the Lodi Revolving Loan Fund for the documentation of the Note and Loan Agreement, secondly to out-of-pocket expenses incurred by the Lodi Revolving Loan Fund on behalf of the applicant.

Loan Fee: As recommended by staff on a case-by-case basis, dependent upon the loan amount requested, the terms of repayment requested and the collateral offered as security for the loan requested. Minimum loan fee is to be one-half (.50) percent of one (1) percent of the loan amount requested; the maximum loan fee to be three (3) percent of the loan amount requested.

Appraisal Fees: RLF Loan borrowers shall arrange and pay for required appraisals.

Out-of –Pocket Expenses: RLF loan borrowers shall pay for out-of-pocket expenses including but not limited to title reports, recording and escrow fees.

Environmental Studies: Environmental Studies/Reports: If real property is offered as collateral for any part of the loan, and environmental study/report (Phase I of Phase II) may be required to ensure that real property is not contaminated. The borrower shall pay costs for the preparation of the environmental study/report.

Closing Costs: Costs associated with the preparation of the Loan Agreement and Note as incurred by the Lodi Revolving Loan Fund, including but not limited to, title reports, recording fees and escrow fees will be charged to the borrower. All costs incurred shall be due and payable to the Revolving Loan Fund.

Modifications: Costs associated with the preparation or modification (which may or may not be granted) of the Note and Loan Agreement as incurred by the Revolving Loan Fund, including, but not limited to attorney fees, title fees, recording fees and escrow fees will be charged to the borrower. All costs incurred shall be due and payable to the Revolving Loan Fund at the time of signing of the modification.

I have read and understand the above schedule of fees and expenses as they pertain to the Lodi Revolving Loan Fund (RLF) financing program.

Date

LOAN APPROVAL AND SUMMARY SHEET

Business Name:

Address:

Business Structure:

**Source and Use
of Funds:**

Source

Use

Repayment Schedule:

Primary Source of Repayment:

Secondary Source of Repayment:

Collateral:

Risk Assessment:

Management Experience:

Competition:

Number of Jobs Created:

Date:

Action Item A-1

To: The Lodi Loan Advisory Committee

From: Wendell Youngsma, San Joaquin County Business Loan Officer

Subject: Recommendation to Approve the Loan Request of

IT IS RECOMMENDED:

1. The
2. The
3. Repayments begin
4. The

BACKGROUND:

MANAGEMENT:

SOURCES AND USES OF FUNDS:

Source

Use

COLLATERAL:

FINANCIAL CHARACTERISTICS:

Personal Income and Expense Analysis
INCOME

EXPENSES

The personal financial statement forconsists of the following (in thousands):

Assets:

Cash
Investments
Vehicles
Household
R/E
Other R/E

Total Assets \$

Liabilities:

Credit Cards
Revolving
Auto
RE

Total Liab. \$
Net Worth \$
Total \$

REASONS FOR RECOMMENDATION:

FISCAL IMPACT:

OTHER MATTERS:

NET CITY COSTS: None.

ACTION TAKEN UPON RECOMMENDATION:

1.
2.

ACTION TAKEN: APPROVED _____ DISAPPROVED _____ OTHER _____

BY: _____ DATE: _____

MOTIONED BY: _____ SECONDED BY: _____

YES: _____ NO: _____

BUSINESS LOAN AGREEMENT

EXHIBIT E

Principal	Loan Date	Maturity	Loan No	Call / Coll	Account	Officer	Initials
\$50,000.00	09-08-2006	09-08-2011					

References in the shaded area are for Lender's use only and do not limit the applicability of this document to any particular loan or item.
Any item above containing "*****" has been omitted due to text length limitations.

Borrower: Joe Borrower
123 Your Street
Stockton, CA 95201

Lender: San Joaquin County Revolving Loan Fund
56 S. Lincoln Street
Stockton, CA 95203

THIS BUSINESS LOAN AGREEMENT dated September 8, 2006, is made and executed between Joe Borrower ("Borrower") and San Joaquin County Revolving Loan Fund ("Lender") on the following terms and conditions. Borrower has received prior commercial loans from Lender or has applied to Lender for a commercial loan or loans or other financial accommodations, including those which may be described on any exhibit or schedule attached to this Agreement ("Loan"). Borrower understands and agrees that: (A) in granting, renewing, or extending any Loan, Lender is relying upon Borrower's representations, warranties, and agreements as set forth in this Agreement; (B) the granting, renewing, or extending of any Loan by Lender at all times shall be subject to Lender's sole judgment and discretion; and (C) all such Loans shall be and remain subject to the terms and conditions of this Agreement.

TERM. This Agreement shall be effective as of September 8, 2006, and shall continue in full force and effect until such time as all of Borrower's Loans in favor of Lender have been paid in full, including principal, interest, costs, expenses, attorneys' fees, and other fees and charges, or until such time as the parties may agree in writing to terminate this Agreement.

CONDITIONS PRECEDENT TO EACH ADVANCE. Lender's obligation to make the initial Advance and each subsequent Advance under this Agreement shall be subject to the fulfillment to Lender's satisfaction of all of the conditions set forth in this Agreement and in the Related Documents.

Loan Documents. Borrower shall provide to Lender the following documents for the Loan: (1) the Note; (2) Security Agreements granting to Lender security interests in the Collateral; (3) financing statements and all other documents perfecting Lender's Security Interests; (4) evidence of insurance as required below; (5) together with all such Related Documents as Lender may require for the Loan; all in form and substance satisfactory to Lender and Lender's counsel.

Payment of Fees and Expenses. Borrower shall have paid to Lender all fees, charges, and other expenses which are then due and payable as specified in this Agreement or any Related Document.

Representations and Warranties. The representations and warranties set forth in this Agreement, in the Related Documents, and in any document or certificate delivered to Lender under this Agreement are true and correct.

No Event of Default. There shall not exist at the time of any Advance a condition which would constitute an Event of Default under this Agreement or under any Related Document.

REPRESENTATIONS AND WARRANTIES. Borrower represents and warrants to Lender, as of the date of this Agreement, as of the date of each disbursement of loan proceeds, as of the date of any renewal, extension or modification of any Loan, and at all times any Indebtedness exists:

Business Activities. Borrower maintains an office at 123 Your Street, Stockton, CA 95201. Unless Borrower has designated otherwise in writing, the principal office is the office at which Borrower keeps its books and records including its records concerning the Collateral. Borrower will notify Lender prior to any change in the location of Borrower's principal office address or any change in Borrower's name. Borrower shall do all things necessary to comply with all regulations, rules, ordinances, statutes, orders and decrees of any governmental or quasi-governmental authority or court applicable to Borrower and Borrower's business activities.

Assumed Business Names. Borrower has filed or recorded all documents or filings required by law relating to all assumed business names used by Borrower. Excluding the name of Borrower, the following is a complete list of all assumed business names under which Borrower does business: None.

Authorization. Borrower's execution, delivery, and performance of this Agreement and all the Related Documents do not conflict with, result in a violation of, or constitute a default under (1) any provision of any agreement or other instrument binding upon Borrower or (2) any law, governmental regulation, court decree, or order applicable to Borrower or to Borrower's properties.

Financial Information. Each of Borrower's financial statements supplied to Lender truly and completely disclosed Borrower's financial condition as of the date of the statement, and there has been no material adverse change in Borrower's financial condition subsequent to the date of the most recent financial statement supplied to Lender. Borrower has no material contingent obligations except as disclosed in such financial statements.

Legal Effect. This Agreement constitutes, and any instrument or agreement Borrower is required to give under this Agreement when delivered will constitute legal, valid, and binding obligations of Borrower enforceable against Borrower in accordance with their respective terms.

Properties. Except as contemplated by this Agreement or as previously disclosed in Borrower's financial statements or in writing to Lender and as accepted by Lender, and except for property tax liens for taxes not presently due and payable, Borrower owns and has good title to all of Borrower's properties free and clear of all Security Interests, and has not executed any security documents or financing statements relating to such properties. All of Borrower's properties are titled in Borrower's legal name, and Borrower has not used or filed a financing statement under any other name for at least the last five (5) years.

Hazardous Substances. Except as disclosed to and acknowledged by Lender in writing, Borrower represents and warrants that: (1) During the period of Borrower's ownership of the Collateral, there has been no use, generation, manufacture, storage, treatment, disposal, release or threatened release of any Hazardous Substance by any person on, under, about or from any of the Collateral. (2) Borrower has no knowledge of, or reason to believe that there has been (a) any breach or violation of any Environmental Laws; (b) any use, generation, manufacture, storage, treatment, disposal, release or threatened release of any Hazardous Substance on, under, about or from the Collateral by any prior owners or occupants of any of the Collateral; or (c) any actual or threatened litigation or claims of any kind by any person relating to such matters. (3) Neither Borrower nor any tenant, contractor, agent or other authorized user of any of the Collateral shall use, generate, manufacture, store, treat, dispose of or release any Hazardous Substance on, under, about or from any of the Collateral; and any such activity shall be conducted in compliance with all applicable federal, state, and local laws, regulations, and ordinances, including without limitation all Environmental Laws. Borrower authorizes Lender and its agents to enter upon the Collateral to make such inspections and tests as Lender may deem appropriate to determine compliance of the Collateral with this section of the Agreement. Any inspections or tests made by Lender shall be at Borrower's expense and for Lender's purposes only and shall not be construed to create any responsibility or liability on the part of Lender to Borrower or to any other person. The representations and warranties contained herein are based on Borrower's due diligence in investigating the Collateral for hazardous waste and Hazardous Substances. Borrower hereby (1) releases and waives any future claims against Lender for indemnity or contribution in the event Borrower becomes liable for cleanup or other costs under any such laws, and (2) agrees to indemnify, defend, and hold

BUSINESS LOAN AGREEMENT (Continued)

Page 2

harmless Lender against any and all claims, losses, liabilities, damages, penalties, and expenses which Lender may directly or indirectly sustain or suffer resulting from a breach of this section of the Agreement or as a consequence of any use, generation, manufacture, storage, disposal, release or threatened release of a hazardous waste or substance on the Collateral. The provisions of this section of the Agreement, including the obligation to indemnify and defend, shall survive the payment of the Indebtedness and the termination, expiration or satisfaction of this Agreement and shall not be affected by Lender's acquisition of any interest in any of the Collateral, whether by foreclosure or otherwise.

Litigation and Claims. No litigation, claim, investigation, administrative proceeding or similar action (including those for unpaid taxes) against Borrower is pending or threatened, and no other event has occurred which may materially adversely affect Borrower's financial condition or properties, other than litigation, claims, or other events, if any, that have been disclosed to and acknowledged by Lender in writing.

Taxes. To the best of Borrower's knowledge, all of Borrower's tax returns and reports that are or were required to be filed, have been filed, and all taxes, assessments and other governmental charges have been paid in full, except those presently being or to be contested by Borrower in good faith in the ordinary course of business and for which adequate reserves have been provided.

Lien Priority. Unless otherwise previously disclosed to Lender in writing, Borrower has not entered into or granted any Security Agreements, or permitted the filing or attachment of any Security Interests on or affecting any of the Collateral directly or indirectly securing repayment of Borrower's Loan and Note, that would be prior or that may in any way be superior to Lender's Security Interests and rights in and to such Collateral.

Binding Effect. This Agreement, the Note, all Security Agreements (if any), and all Related Documents are binding upon the signers thereof, as well as upon their successors, representatives and assigns, and are legally enforceable in accordance with their respective terms.

AFFIRMATIVE COVENANTS. Borrower covenants and agrees with Lender that, so long as this Agreement remains in effect, Borrower will:

Notices of Claims and Litigation. Promptly inform Lender in writing of (1) all material adverse changes in Borrower's financial condition, and (2) all existing and all threatened litigation, claims, investigations, administrative proceedings or similar actions affecting Borrower or any Guarantor which could materially affect the financial condition of Borrower or the financial condition of any Guarantor.

Financial Records. Maintain its books and records in accordance with GAAP, applied on a consistent basis, and permit Lender to examine and audit Borrower's books and records at all reasonable times.

Financial Statements. Furnish Lender with such financial statements and other related information at such frequencies and in such detail as Lender may reasonably request.

Additional Information. Furnish such additional information and statements, as Lender may request from time to time.

Insurance. Maintain fire and other risk insurance, public liability insurance, and such other insurance as Lender may require with respect to Borrower's properties and operations, in form, amounts, coverages and with insurance companies acceptable to Lender. Borrower, upon request of Lender, will deliver to Lender from time to time the policies or certificates of insurance in form satisfactory to Lender, including stipulations that coverages will not be cancelled or diminished without at least ten (10) days prior written notice to Lender. Each insurance policy also shall include an endorsement providing that coverage in favor of Lender will not be impaired in any way by any act, omission or default of Borrower or any other person. In connection with all policies covering assets in which Lender holds or is offered a security interest for the Loans, Borrower will provide Lender with such lender's loss payable or other endorsements as Lender may require.

Insurance Reports. Furnish to Lender, upon request of Lender, reports on each existing insurance policy showing such information as Lender may reasonably request, including without limitation the following: (1) the name of the insurer; (2) the risks insured; (3) the amount of the policy; (4) the properties insured; (5) the then current property values on the basis of which insurance has been obtained, and the manner of determining those values; and (6) the expiration date of the policy. In addition, upon request of Lender (however not more often than annually), Borrower will have an independent appraiser satisfactory to Lender determine, as applicable, the actual cash value or replacement cost of any Collateral. The cost of such appraisal shall be paid by Borrower.

Other Agreements. Comply with all terms and conditions of all other agreements, whether now or hereafter existing, between Borrower and any other party and notify Lender immediately in writing of any default in connection with any other such agreements.

Loan Proceeds. Use all Loan proceeds solely for Borrower's business operations, unless specifically consented to the contrary by Lender in writing.

Taxes, Charges and Liens. Pay and discharge when due all of its indebtedness and obligations, including without limitation all assessments, taxes, governmental charges, levies and liens, of every kind and nature, imposed upon Borrower or its properties, income, or profits, prior to the date on which penalties would attach, and all lawful claims that, if unpaid, might become a lien or charge upon any of Borrower's properties, income, or profits.

Performance. Perform and comply, in a timely manner, with all terms, conditions, and provisions set forth in this Agreement, in the Related Documents, and in all other instruments and agreements between Borrower and Lender. Borrower shall notify Lender immediately in writing of any default in connection with any agreement.

Operations. Maintain executive and management personnel with substantially the same qualifications and experience as the present executive and management personnel; provide written notice to Lender of any change in executive and management personnel; conduct its business affairs in a reasonable and prudent manner.

Environmental Studies. Promptly conduct and complete, at Borrower's expense, all such investigations, studies, samplings and testings as may be requested by Lender or any governmental authority relative to any substance, or any waste or by-product of any substance defined as toxic or a hazardous substance under applicable federal, state, or local law, rule, regulation, order or directive, at or affecting any property or any facility owned, leased or used by Borrower.

Compliance with Governmental Requirements. Comply with all laws, ordinances, and regulations, now or hereafter in effect, of all governmental authorities applicable to the conduct of Borrower's properties, businesses and operations, and to the use or occupancy of the Collateral, including without limitation, the Americans With Disabilities Act. Borrower may contest in good faith any such law, ordinance, or regulation and withhold compliance during any proceeding, including appropriate appeals, so long as Borrower has notified Lender in writing prior to doing so and so long as, in Lender's sole opinion, Lender's interests in the Collateral are not jeopardized. Lender may require Borrower to post adequate security or a surety bond, reasonably satisfactory to Lender, to protect Lender's interest.

Inspection. Permit employees or agents of Lender at any reasonable time to inspect any and all Collateral for the Loan or Loans and Borrower's other properties and to examine or audit Borrower's books, accounts, and records and to make copies and memoranda of Borrower's books, accounts, and records. If Borrower now or at any time hereafter maintains any records (including without limitation computer generated records and computer software programs for the generation of such records) in the possession of a third party, Borrower, upon request of Lender, shall notify such party to permit Lender free access to such records at all reasonable times and to provide Lender with copies of any records it may request, all at Borrower's expense.

BUSINESS LOAN AGREEMENT (Continued)

Page 3

Environmental Compliance and Reports. Borrower shall comply in all respects with any and all Environmental Laws; not cause or permit to exist, as a result of an intentional or unintentional action or omission on Borrower's part or on the part of any third party, on property owned and/or occupied by Borrower, any environmental activity where damage may result to the environment, unless such environmental activity is pursuant to and in compliance with the conditions of a permit issued by the appropriate federal, state or local governmental authorities; shall furnish to Lender promptly and in any event within thirty (30) days after receipt thereof a copy of any notice, summons, lien, citation, directive, letter or other communication from any governmental agency or instrumentality concerning any intentional or unintentional action or omission on Borrower's part in connection with any environmental activity whether or not there is damage to the environment and/or other natural resources.

Additional Assurances. Make, execute and deliver to Lender such promissory notes, mortgages, deeds of trust, security agreements, assignments, financing statements, instruments, documents and other agreements as Lender or its attorneys may reasonably request to evidence and secure the Loans and to perfect all Security Interests.

RECOVERY OF ADDITIONAL COSTS. If the imposition of or any change in any law, rule, regulation or guideline, or the interpretation or application of any thereof by any court or administrative or governmental authority (including any request or policy not having the force of law) shall impose, modify or make applicable any taxes (except federal, state or local income or franchise taxes imposed on Lender), reserve requirements, capital adequacy requirements or other obligations which would (A) increase the cost to Lender for extending or maintaining the credit facilities to which this Agreement relates, (B) reduce the amounts payable to Lender under this Agreement or the Related Documents, or (C) reduce the rate of return on Lender's capital as a consequence of Lender's obligations with respect to the credit facilities to which this Agreement relates, then Borrower agrees to pay Lender such additional amounts as will compensate Lender therefor, within five (5) days after Lender's written demand for such payment, which demand shall be accompanied by an explanation of such imposition or charge and a calculation in reasonable detail of the additional amounts payable by Borrower, which explanation and calculations shall be conclusive in the absence of manifest error.

LENDER'S EXPENDITURES. If any action or proceeding is commenced that would materially affect Lender's interest in the Collateral or if Borrower fails to comply with any provision of this Agreement or any Related Documents, including but not limited to Borrower's failure to discharge or pay when due any amounts Borrower is required to discharge or pay under this Agreement or any Related Documents, Lender on Borrower's behalf may (but shall not be obligated to) take any action that Lender deems appropriate, including but not limited to discharging or paying all taxes, liens, security interests, encumbrances and other claims, at any time levied or placed on any Collateral and paying all costs for insuring, maintaining and preserving any Collateral. All such expenditures incurred or paid by Lender for such purposes will then bear interest at the rate charged under the Note from the date incurred or paid by Lender to the date of repayment by Borrower. All such expenses will become a part of the Indebtedness and, at Lender's option, will (A) be payable on demand; (B) be added to the balance of the Note and be apportioned among and be payable with any installment payments to become due during either (1) the term of any applicable insurance policy; or (2) the remaining term of the Note; or (C) be treated as a balloon payment which will be due and payable at the Note's maturity.

NEGATIVE COVENANTS. Borrower covenants and agrees with Lender that while this Agreement is in effect, Borrower shall not, without the prior written consent of Lender:

Indebtedness and Liens. (1) Except for trade debt incurred in the normal course of business and indebtedness to Lender contemplated by this Agreement, create, incur or assume indebtedness for borrowed money, including capital leases, (2) sell, transfer, mortgage, assign, pledge, lease, grant a security interest in, or encumber any of Borrower's assets (except as allowed as Permitted Liens), or (3) sell with recourse any of Borrower's accounts, except to Lender.

Continuity of Operations. (1) Engage in any business activities substantially different than those in which Borrower is presently engaged, or (2) cease operations, liquidate, merge, transfer, acquire or consolidate with any other entity, change ownership, dissolve or transfer or sell Collateral out of the ordinary course of business.

Loans, Acquisitions and Guaranties. (1) Loan, invest in or advance money or assets to any other person, enterprise or entity, (2) purchase, create or acquire any interest in any other enterprise or entity, or (3) incur any obligation as surety or guarantor other than in the ordinary course of business.

Agreements. Borrower will not enter into any agreement containing any provisions which would be violated or breached by the performance of Borrower's obligations under this Agreement or in connection herewith.

CESSATION OF ADVANCES. If Lender has made any commitment to make any Loan to Borrower, whether under this Agreement or under any other agreement, Lender shall have no obligation to make Loan Advances or to disburse Loan proceeds if: (A) Borrower or any Guarantor is in default under the terms of this Agreement or any of the Related Documents or any other agreement that Borrower or any Guarantor has with Lender; (B) Borrower or any Guarantor dies, becomes incompetent or becomes insolvent, files a petition in bankruptcy or similar proceedings, or is adjudged a bankrupt; (C) there occurs a material adverse change in Borrower's financial condition, in the financial condition of any Guarantor, or in the value of any Collateral securing any Loan; or (D) any Guarantor seeks, claims or otherwise attempts to limit, modify or revoke such Guarantor's guaranty of the Loan or any other loan with Lender; or (E) Lender in good faith deems itself insecure, even though no Event of Default shall have occurred.

DEFAULT. Each of the following shall constitute an Event of Default under this Agreement:

Payment Default. Borrower fails to make any payment when due under the Loan.

Other Defaults. Borrower fails to comply with or to perform any other term, obligation, covenant or condition contained in this Agreement or in any of the Related Documents or to comply with or to perform any term, obligation, covenant or condition contained in any other agreement between Lender and Borrower.

False Statements. Any warranty, representation or statement made or furnished to Lender by Borrower or on Borrower's behalf under this Agreement or the Related Documents is false or misleading in any material respect, either now or at the time made or furnished or becomes false or misleading at any time thereafter.

Death or Insolvency. The death of Borrower or the dissolution or termination of Borrower's existence as a going business, the insolvency of Borrower, the appointment of a receiver for any part of Borrower's property, any assignment for the benefit of creditors, any type of creditor workout, or the commencement of any proceeding under any bankruptcy or insolvency laws by or against Borrower.

Defective Collateralization. This Agreement or any of the Related Documents ceases to be in full force and effect (including failure of any collateral document to create a valid and perfected security interest or lien) at any time and for any reason.

Creditor or Forfeiture Proceedings. Commencement of foreclosure or forfeiture proceedings, whether by judicial proceeding, self-help, repossession or any other method, by any creditor of Borrower or by any governmental agency against any collateral securing the Loan. This includes a garnishment of any of Borrower's accounts, including deposit accounts, with Lender. However, this Event of Default shall not apply if there is a good faith dispute by Borrower as to the validity or reasonableness of the claim which is the basis of the creditor or forfeiture proceeding and if Borrower gives Lender written notice of the creditor or forfeiture proceeding and deposits with Lender monies or a surety bond for the creditor or forfeiture proceeding, in an amount determined by Lender, in its sole discretion, as being an adequate reserve or bond for the dispute.

Events Affecting Guarantor. Any of the preceding events occurs with respect to any Guarantor of any of the Indebtedness or any Guarantor dies

BUSINESS LOAN AGREEMENT (Continued)

or becomes incompetent, or revokes or disputes the validity of, or liability under, any Guaranty of the Indebtedness.

Adverse Change. A material adverse change occurs in Borrower's financial condition, or Lender believes the prospect of payment or performance of the Loan is impaired.

Insecurity. Lender in good faith believes itself insecure.

EFFECT OF AN EVENT OF DEFAULT. If any Event of Default shall occur, except where otherwise provided in this Agreement or the Related Documents, all commitments and obligations of Lender under this Agreement or the Related Documents or any other agreement immediately will terminate (including any obligation to make further Loan Advances or disbursements), and, at Lender's option, all Indebtedness immediately will become due and payable, all without notice of any kind to Borrower, except that in the case of an Event of Default of the type described in the "Insolvency" subsection above, such acceleration shall be automatic and not optional. In addition, Lender shall have all the rights and remedies provided in the Related Documents or available at law, in equity, or otherwise. Except as may be prohibited by applicable law, all of Lender's rights and remedies shall be cumulative and may be exercised singularly or concurrently. Election by Lender to pursue any remedy shall not exclude pursuit of any other remedy, and an election to make expenditures or to take action to perform an obligation of Borrower or of any Grantor shall not affect Lender's right to declare a default and to exercise its rights and remedies.

BUSINESS LOAN AGREEMENT EXHIBIT. An exhibit, titled "Compliance with Federal Law," is attached to this Agreement and by this reference is made a part of this Agreement just as if all the provisions, terms and conditions of the Exhibit had been fully set forth in this Agreement.

MISCELLANEOUS PROVISIONS. The following miscellaneous provisions are a part of this Agreement:

Amendments. This Agreement, together with any Related Documents, constitutes the entire understanding and agreement of the parties as to the matters set forth in this Agreement. No alteration of or amendment to this Agreement shall be effective unless given in writing and signed by the party or parties sought to be charged or bound by the alteration or amendment.

Attorneys' Fees; Expenses. Borrower agrees to pay upon demand all of Lender's costs and expenses, including Lender's attorneys' fees and Lender's legal expenses, incurred in connection with the enforcement of this Agreement. Lender may hire or pay someone else to help enforce this Agreement, and Borrower shall pay the costs and expenses of such enforcement. Costs and expenses include Lender's attorneys' fees and legal expenses whether or not there is a lawsuit, including attorneys' fees and legal expenses for bankruptcy proceedings (including efforts to modify or vacate any automatic stay or injunction), appeals, and any anticipated post-judgment collection services. Borrower also shall pay all court costs and such additional fees as may be directed by the court.

Caption Headings. Caption headings in this Agreement are for convenience purposes only and are not to be used to interpret or define the provisions of this Agreement.

Consent to Loan Participation. Borrower agrees and consents to Lender's sale or transfer, whether now or later, of one or more participation interests in the Loan to one or more purchasers, whether related or unrelated to Lender. Lender may provide, without any limitation whatsoever, to any one or more purchasers, or potential purchasers, any information or knowledge Lender may have about Borrower or about any other matter relating to the Loan, and Borrower hereby waives any rights to privacy Borrower may have with respect to such matters. Borrower additionally waives any and all notices of sale of participation interests, as well as all notices of any repurchase of such participation interests. Borrower also agrees that the purchasers of any such participation interests will be considered as the absolute owners of such interests in the Loan and will have all the rights granted under the participation agreement or agreements governing the sale of such participation interests. Borrower further waives all rights of offset or counterclaim that it may have now or later against Lender or against any purchaser of such a participation interest and unconditionally agrees that either Lender or such purchaser may enforce Borrower's obligation under the Loan irrespective of the failure or insolvency of any holder of any interest in the Loan. Borrower further agrees that the purchaser of any such participation interests may enforce its interests irrespective of any personal claims or defenses that Borrower may have against Lender.

Governing Law. This Agreement will be governed by federal law applicable to Lender and, to the extent not preempted by federal law, the laws of the State of California without regard to its conflicts of law provisions. This Agreement has been accepted by Lender in the State of California.

No Waiver by Lender. Lender shall not be deemed to have waived any rights under this Agreement unless such waiver is given in writing and signed by Lender. No delay or omission on the part of Lender in exercising any right shall operate as a waiver of such right or any other right. A waiver by Lender of a provision of this Agreement shall not prejudice or constitute a waiver of Lender's right otherwise to demand strict compliance with that provision or any other provision of this Agreement. No prior waiver by Lender, nor any course of dealing between Lender and Borrower, or between Lender and any Grantor, shall constitute a waiver of any of Lender's rights or of any of Borrower's or any Grantor's obligations as to any future transactions. Whenever the consent of Lender is required under this Agreement, the granting of such consent by Lender in any instance shall not constitute continuing consent to subsequent instances where such consent is required and in all cases such consent may be granted or withheld in the sole discretion of Lender.

Notices. Any notice required to be given under this Agreement shall be given in writing, and shall be effective when actually delivered, when actually received by telefacsimile (unless otherwise required by law), when deposited with a nationally recognized overnight courier, or, if mailed, when deposited in the United States mail, as first class, certified or registered mail postage prepaid, directed to the addresses shown near the beginning of this Agreement. Any party may change its address for notices under this Agreement by giving formal written notice to the other parties, specifying that the purpose of the notice is to change the party's address. For notice purposes, Borrower agrees to keep Lender informed at all times of Borrower's current address. Unless otherwise provided or required by law, if there is more than one Borrower, any notice given by Lender to any Borrower is deemed to be notice given to all Borrowers.

Severability. If a court of competent jurisdiction finds any provision of this Agreement to be illegal, invalid, or unenforceable as to any circumstance, that finding shall not make the offending provision illegal, invalid, or unenforceable as to any other circumstance. If feasible, the offending provision shall be considered modified so that it becomes legal, valid and enforceable. If the offending provision cannot be so modified, it shall be considered deleted from this Agreement. Unless otherwise required by law, the illegality, invalidity, or unenforceability of any provision of this Agreement shall not affect the legality, validity or enforceability of any other provision of this Agreement.

Successors and Assigns. All covenants and agreements by or on behalf of Borrower contained in this Agreement or any Related Documents shall bind Borrower's successors and assigns and shall inure to the benefit of Lender and its successors and assigns. Borrower shall not, however, have the right to assign Borrower's rights under this Agreement or any interest therein, without the prior written consent of Lender.

Survival of Representations and Warranties. Borrower understands and agrees that in making the Loan, Lender is relying on all representations, warranties, and covenants made by Borrower in this Agreement or in any certificate or other instrument delivered by Borrower to Lender under this Agreement or the Related Documents. Borrower further agrees that regardless of any investigation made by Lender, all such representations, warranties and covenants will survive the making of the Loan and delivery to Lender of the Related Documents, shall be continuing in nature, and shall remain in full force and effect until such time as Borrower's Indebtedness shall be paid in full, or until this Agreement shall be terminated in the manner provided above, whichever is the last to occur.

BUSINESS LOAN AGREEMENT (Continued)

Time is of the Essence. Time is of the essence in the performance of this Agreement.

Waive Jury. To the extent permitted by applicable law, all parties to this Agreement hereby waive the right to any jury trial in any action, proceeding, or counterclaim brought by any party against any other party.

DEFINITIONS. The following capitalized words and terms shall have the following meanings when used in this Agreement. Unless specifically stated to the contrary, all references to dollar amounts shall mean amounts in lawful money of the United States of America. Words and terms used in the singular shall include the plural, and the plural shall include the singular, as the context may require. Words and terms not otherwise defined in this Agreement shall have the meanings attributed to such terms in the Uniform Commercial Code. Accounting words and terms not otherwise defined in this Agreement shall have the meanings assigned to them in accordance with generally accepted accounting principles as in effect on the date of this Agreement:

Advance. The word "Advance" means a disbursement of Loan funds made, or to be made, to Borrower or on Borrower's behalf on a line of credit or multiple advance basis under the terms and conditions of this Agreement.

Agreement. The word "Agreement" means this Business Loan Agreement, as this Business Loan Agreement may be amended or modified from time to time, together with all exhibits and schedules attached to this Business Loan Agreement from time to time.

Borrower. The word "Borrower" means Joe Borrower and includes all co-signers and co-makers signing the Note and all their successors and assigns.

Collateral. The word "Collateral" means all property and assets granted as collateral security for a Loan, whether real or personal property, whether granted directly or indirectly, whether granted now or in the future, and whether granted in the form of a security interest, mortgage, collateral mortgage, deed of trust, assignment, pledge, crop pledge, chattel mortgage, collateral chattel mortgage, chattel trust, factor's lien, equipment trust, conditional sale, trust receipt, lien, charge, lien or title retention contract, lease or consignment intended as a security device, or any other security or lien interest whatsoever, whether created by law, contract, or otherwise.

Environmental Laws. The words "Environmental Laws" mean any and all state, federal and local statutes, regulations and ordinances relating to the protection of human health or the environment, including without limitation the Comprehensive Environmental Response, Compensation, and Liability Act of 1980, as amended, 42 U.S.C. Section 9601, et seq. ("CERCLA"), the Superfund Amendments and Reauthorization Act of 1986, Pub. L. No. 99-499 ("SARA"), the Hazardous Materials Transportation Act, 49 U.S.C. Section 1801, et seq., the Resource Conservation and Recovery Act, 42 U.S.C. Section 6901, et seq., Chapters 6.5 through 7.7 of Division 20 of the California Health and Safety Code, Section 25100, et seq., or other applicable state or federal laws, rules, or regulations adopted pursuant thereto.

Event of Default. The words "Event of Default" mean any of the events of default set forth in this Agreement in the default section of this Agreement.

GAAP. The word "GAAP" means generally accepted accounting principles.

Grantor. The word "Grantor" means each and all of the persons or entities granting a Security Interest in any Collateral for the Loan, including without limitation all Borrowers granting such a Security Interest.

Guarantor. The word "Guarantor" means any guarantor, surety, or accommodation party of any or all of the Loan.

Guaranty. The word "Guaranty" means the guaranty from Guarantor to Lender, including without limitation a guaranty of all or part of the Note.

Hazardous Substances. The words "Hazardous Substances" mean materials that, because of their quantity, concentration or physical, chemical or infectious characteristics, may cause or pose a present or potential hazard to human health or the environment when improperly used, treated, stored, disposed of, generated, manufactured, transported or otherwise handled. The words "Hazardous Substances" are used in their very broadest sense and include without limitation any and all hazardous or toxic substances, materials or waste as defined by or listed under the Environmental Laws. The term "Hazardous Substances" also includes, without limitation, petroleum and petroleum by-products or any fraction thereof and asbestos.

Indebtedness. The word "Indebtedness" means the indebtedness evidenced by the Note or Related Documents, including all principal and interest together with all other indebtedness and costs and expenses for which Borrower is responsible under this Agreement or under any of the Related Documents.

Lender. The word "Lender" means San Joaquin County Revolving Loan Fund, its successors and assigns.

Loan. The word "Loan" means any and all loans and financial accommodations from Lender to Borrower whether now or hereafter existing, and however evidenced, including without limitation those loans and financial accommodations described herein or described on any exhibit or schedule attached to this Agreement from time to time.

Note. The word "Note" means the Note executed by Joe Borrower in the principal amount of \$50,000.00 dated September 8, 2006, together with all renewals of, extensions of, modifications of, refinancings of, consolidations of, and substitutions for the note or credit agreement.

Permitted Liens. The words "Permitted Liens" mean (1) liens and security interests securing Indebtedness owed by Borrower to Lender; (2) liens for taxes, assessments, or similar charges either not yet due or being contested in good faith; (3) liens of materialmen, mechanics, warehousemen, or carriers, or other like liens arising in the ordinary course of business and securing obligations which are not yet delinquent; (4) purchase money liens or purchase money security interests upon or in any property acquired or held by Borrower in the ordinary course of business to secure indebtedness outstanding on the date of this Agreement or permitted to be incurred under the paragraph of this Agreement titled "Indebtedness and Liens"; (5) liens and security interests which, as of the date of this Agreement, have been disclosed to and approved by the Lender in writing; and (6) those liens and security interests which in the aggregate constitute an immaterial and insignificant monetary amount with respect to the net value of Borrower's assets.

Related Documents. The words "Related Documents" mean all promissory notes, credit agreements, loan agreements, environmental agreements, guaranties, security agreements, mortgages, deeds of trust, security deeds, collateral mortgages, and all other instruments, agreements and documents, whether now or hereafter existing, executed in connection with the Loan.

Security Agreement. The words "Security Agreement" mean and include without limitation any agreements, promises, covenants, arrangements, understandings or other agreements, whether created by law, contract, or otherwise, evidencing, governing, representing, or creating a Security Interest.

Security Interest. The words "Security Interest" mean, without limitation, any and all types of collateral security, present and future, whether in the form of a lien, charge, encumbrance, mortgage, deed of trust, security deed, assignment, pledge, crop pledge, chattel mortgage, collateral chattel mortgage, chattel trust, factor's lien, equipment trust, conditional sale, trust receipt, lien or title retention contract, lease or consignment intended as a security device, or any other security or lien interest whatsoever whether created by law, contract, or otherwise.

**BUSINESS LOAN AGREEMENT
(Continued)**

Page 6

BORROWER ACKNOWLEDGES HAVING READ ALL THE PROVISIONS OF THIS BUSINESS LOAN AGREEMENT AND BORROWER AGREES TO ITS TERMS. THIS BUSINESS LOAN AGREEMENT IS DATED SEPTEMBER 8, 2006.

BORROWER:

X

Joe Borrower

LENDER:

SAN JOAQUIN COUNTY REVOLVING LOAN FUND

By:

Authorized Signer

EXHIBIT A

COMPLIANCE WITH FEDERAL LAW

Borrower will protect and hold the Federal Government harmless from and against all liabilities that the Federal Government may incur as a result of providing an award to assist (directly or indirectly) in site preparation or construction as well as the renovation or repair of any facility or site. This applies to the extent that such liabilities are incurred because of ground water, surface, soil or other conditions caused by operations of the Borrower or any of its predecessors on the property.

Borrower will comply with all applicable federal regulations and statutes and with the requirements of the federal sponsoring agency concerning special requirements of the law, program requirements, and other administrative requirements, as set forth in the Economic Development Administration of the United States Department of Commerce ("EDA") publications: "U.S. Department of Commerce Economic Development Administration Revolving Loan Fund Standard Terms and Conditions," including, without limitations:

1. **Pre-loan Requirements** Borrowers must comply with applicable laws and regulations including but not limited to 13 CFR §§ 316.1, 316.3, 316.7, 316.8, 316.15, and 317.
2. **Non-Discrimination Requirements** No person in the United States shall on the grounds of race, color, national origin, handicap, age, religion, or sex be excluded from participation in, be denied the benefits of, or be subject to discrimination under any program or activity receiving Federal financial assistance. The borrower agrees to comply with the non-discrimination statutory provisions below
 - a) Title VI of the Civil Rights Act of 1964 (42 USC § 2000d) and DoC implementing regulations published at 15 CFR Part 8 which prohibit discrimination on the grounds of race, color, or national origin under programs or activities receiving Federal financial assistance
 - b) Title IX of the Education Amendments of 1972 (20 U.S.C. § 1681 et seq.) prohibiting discrimination on the basis of sex under Federally assisted education programs or activities;
 - c) Section 504 of the Rehabilitation Act of 1973, as amended (29 U.S.C. § 794) and DoC implementing regulations published at 15 CFR Part 8b prohibiting discrimination on the basis of handicap under any program or activity receiving or benefiting from Federal assistance;
 - d) The Age Discrimination Act of 1975, as amended (42 U.S.C. § 6101 et seq.) and DoC implementing regulations published at 15 CFR Part 20 prohibiting discrimination on the basis of age in programs or activities receiving Federal financial assistance;
 - e) The Americans with Disabilities Act of 1990 (42 U.S.C. § 12101 et seq.) prohibiting discrimination on the basis of disability under programs, activities, and services provided or made available by state and local governments or provide public transportation;
 - f) Section 112 of P.L. 92-65 (42 U.S.C. § 3123) prohibiting sex discrimination in any program or activity receiving Federal financial assistance under PWEDA.
 - g) Any other applicable non-discrimination law(s).
3. **Davis Bacon Act** In accordance with section 602 of PWEDA, all laborers and mechanics employed by contractors or subcontractors on projects assisted by EDA under PWEDA shall be paid in accordance with the Davis-Bacon Act, as amended (40 U.S.C. 276a – 276a-5)

Initial _____

Initial _____

COMMERCIAL SECURITY AGREEMENT

Principal	Loan Date	Maturity	Loan No	Call / Coll	Account	Officer	Initials
\$50,000.00	09-08-2006	09-08-2011					

References in the shaded area are for Lender's use only and do not limit the applicability of this document to any particular loan or item.
Any item above containing "*****" has been omitted due to text length limitations.

Grantor: Joe Borrower
123 Your Street
Stockton, CA 95201

Lender: San Joaquin County Revolving Loan Fund
56 S. Lincoln Street
Stockton, CA 95203

THIS COMMERCIAL SECURITY AGREEMENT dated September 8, 2006, is made and executed between Joe Borrower ("Grantor") and San Joaquin County Revolving Loan Fund ("Lender").

GRANT OF SECURITY INTEREST. For valuable consideration, Grantor grants to Lender a security interest in the Collateral to secure the indebtedness and agrees that Lender shall have the rights stated in this Agreement with respect to the Collateral, in addition to all other rights which Lender may have by law.

COLLATERAL DESCRIPTION. The word "Collateral" as used in this Agreement means the following described property, whether now owned or hereafter acquired, whether now existing or hereafter arising, and wherever located, in which Grantor is giving to Lender a security interest for the payment of the indebtedness and performance of all other obligations under the Note and this Agreement:

All inventory, equipment, accounts (including but not limited to all health-care-insurance receivables), chattel paper, instruments (including but not limited to all promissory notes), letter-of-credit rights, letters of credit, documents, deposit accounts, investment property, money, other rights to payment and performance, and general intangibles (including but not limited to all software and all payment intangibles); all fixtures; all attachments, accessions, accessories, fittings, increases, tools, parts, repairs, supplies, and commingled goods relating to the foregoing property, and all additions, replacements of and substitutions for all or any part of the foregoing property; all insurance refunds relating to the foregoing property; all good will relating to the foregoing property; all records and data and embedded software relating to the foregoing property, and all equipment, inventory and software to utilize, create, maintain and process any such records and data on electronic media; and all supporting obligations relating to the foregoing property; all whether now existing or hereafter arising, whether now owned or hereafter acquired or whether now or hereafter subject to any rights in the foregoing property; and all products and proceeds (including but not limited to all insurance payments) of or relating to the foregoing property.

In addition, the word "Collateral" also includes all the following, whether now owned or hereafter acquired, whether now existing or hereafter arising, and wherever located:

- (A) All accessions, attachments, accessories, tools, parts, supplies, replacements of and additions to any of the collateral described herein, whether added now or later.
- (B) All products and produce of any of the property described in this Collateral section.
- (C) All accounts, general intangibles, instruments, rents, monies, payments, and all other rights, arising out of a sale, lease, consignment or other disposition of any of the property described in this Collateral section.
- (D) All proceeds (including insurance proceeds) from the sale, destruction, loss, or other disposition of any of the property described in this Collateral section, and sums due from a third party who has damaged or destroyed the Collateral or from that party's insurer, whether due to judgment, settlement or other process.
- (E) All records and data relating to any of the property described in this Collateral section, whether in the form of a writing, photograph, microfilm, microfiche, or electronic media, together with all of Grantor's right, title, and interest in and to all computer software required to utilize, create, maintain, and process any such records or data on electronic media.

Some or all of the Collateral may be located on the following described real estate:

123 Your Street, Stockton, Ca. 95201

GRANTOR'S REPRESENTATIONS AND WARRANTIES WITH RESPECT TO THE COLLATERAL. With respect to the Collateral, Grantor represents and promises to Lender that:

Perfection of Security Interest. Grantor agrees to take whatever actions are requested by Lender to perfect and continue Lender's security interest in the Collateral. Upon request of Lender, Grantor will deliver to Lender any and all of the documents evidencing or constituting the Collateral, and Grantor will note Lender's interest upon any and all chattel paper and instruments if not delivered to Lender for possession by Lender.

Notices to Lender. Grantor will promptly notify Lender in writing at Lender's address shown above (or such other addresses as Lender may designate from time to time) prior to any (1) change in Grantor's name; (2) change in Grantor's assumed business name(s); (3) change in the authorized signer(s); (4) change in Grantor's principal office address; (5) change in Grantor's principal residence; (6) conversion of Grantor to a new or different type of business entity; or (7) change in any other aspect of Grantor that directly or indirectly relates to any agreements between Grantor and Lender. No change in Grantor's name or principal residence will take effect until after Lender has received notice.

No Violation. The execution and delivery of this Agreement will not violate any law or agreement governing Grantor or to which Grantor is a party.

Enforceability of Collateral. To the extent the Collateral consists of accounts, chattel paper, or general intangibles, as defined by the Uniform Commercial Code, the Collateral is enforceable in accordance with its terms, is genuine, and fully complies with all applicable laws and regulations concerning form, content and manner of preparation and execution, and all persons appearing to be obligated on the Collateral have authority and capacity to contract and are in fact obligated as they appear to be on the Collateral. At the time any account becomes subject to a security interest in favor of Lender, the account shall be a good and valid account representing an undisputed, bona fide indebtedness incurred by the account debtor, for merchandise held subject to delivery instructions or previously shipped or delivered pursuant to a contract of sale, or for services previously performed by Grantor with or for the account debtor. So long as this Agreement remains in effect, Grantor shall not, without Lender's prior written consent, compromise, settle, adjust, or extend payment under or with regard to any such Accounts. There shall be no setoffs or counterclaims against any of the Collateral, and no agreement shall have been made under which any deductions or discounts may be claimed concerning the Collateral except those disclosed to Lender in writing.

Location of the Collateral. Except in the ordinary course of Grantor's business, Grantor agrees to keep the Collateral (or to the extent the Collateral consists of intangible property such as accounts or general intangibles, the records concerning the Collateral) at Grantor's address

COMMERCIAL SECURITY AGREEMENT (Continued)

shown above or at such other locations as are acceptable to Lender. Upon Lender's request, Grantor will deliver to Lender in form satisfactory to Lender a schedule of real properties and Collateral locations relating to Grantor's operations, including without limitation the following: (1) all real property Grantor owns or is purchasing; (2) all real property Grantor is renting or leasing; (3) all storage facilities Grantor owns, rents, leases, or uses; and (4) all other properties where Collateral is or may be located.

Removal of the Collateral. Except in the ordinary course of Grantor's business, including the sales of inventory, Grantor shall not remove the Collateral from its existing location without Lender's prior written consent. To the extent that the Collateral consists of vehicles, or other titled property, Grantor shall not take or permit any action which would require application for certificates of title for the vehicles outside the State of California, without Lender's prior written consent. Grantor shall, whenever requested, advise Lender of the exact location of the Collateral.

Transactions Involving Collateral. Except for inventory sold or accounts collected in the ordinary course of Grantor's business, or as otherwise provided for in this Agreement, Grantor shall not sell, offer to sell, or otherwise transfer or dispose of the Collateral. While Grantor is not in default under this Agreement, Grantor may sell inventory, but only in the ordinary course of its business and only to buyers who qualify as a buyer in the ordinary course of business. A sale in the ordinary course of Grantor's business does not include a transfer in partial or total satisfaction of a debt or any bulk sale. Grantor shall not pledge, mortgage, encumber or otherwise permit the Collateral to be subject to any lien, security interest, encumbrance, or charge, other than the security interest provided for in this Agreement, without the prior written consent of Lender. This includes security interests even if junior in right to the security interests granted under this Agreement. Unless waived by Lender, all proceeds from any disposition of the Collateral (for whatever reason) shall be held in trust for Lender and shall not be commingled with any other funds; provided however, this requirement shall not constitute consent by Lender to any sale or other disposition. Upon receipt, Grantor shall immediately deliver any such proceeds to Lender.

Title. Grantor represents and warrants to Lender that Grantor holds good and marketable title to the Collateral, free and clear of all liens and encumbrances except for the lien of this Agreement. No financing statement covering any of the Collateral is on file in any public office other than those which reflect the security interest created by this Agreement or to which Lender has specifically consented. Grantor shall defend Lender's rights in the Collateral against the claims and demands of all other persons.

Repairs and Maintenance. Grantor agrees to keep and maintain, and to cause others to keep and maintain, the Collateral in good order, repair and condition at all times while this Agreement remains in effect. Grantor further agrees to pay when due all claims for work done on, or services rendered or material furnished in connection with the Collateral so that no lien or encumbrance may ever attach to or be filed against the Collateral.

Inspection of Collateral. Lender and Lender's designated representatives and agents shall have the right at all reasonable times to examine and inspect the Collateral wherever located.

Taxes, Assessments and Liens. Grantor will pay when due all taxes, assessments and liens upon the Collateral, its use or operation, upon this Agreement, upon any promissory note or notes evidencing the Indebtedness, or upon any of the other Related Documents. Grantor may withhold any such payment or may elect to contest any lien if Grantor is in good faith conducting an appropriate proceeding to contest the obligation to pay and so long as Lender's interest in the Collateral is not jeopardized in Lender's sole opinion. If the Collateral is subjected to a lien which is not discharged within fifteen (15) days, Grantor shall deposit with Lender cash, a sufficient corporate surety bond or other security satisfactory to Lender in an amount adequate to provide for the discharge of the lien plus any interest, costs, attorneys' fees or other charges that could accrue as a result of foreclosure or sale of the Collateral. In any contest Grantor shall defend itself and Lender and shall satisfy any final adverse judgment before enforcement against the Collateral. Grantor shall name Lender as an additional obligee under any surety bond furnished in the contest proceedings. Grantor further agrees to furnish Lender with evidence that such taxes, assessments, and governmental and other charges have been paid in full and in a timely manner. Grantor may withhold any such payment or may elect to contest any lien if Grantor is in good faith conducting an appropriate proceeding to contest the obligation to pay and so long as Lender's interest in the Collateral is not jeopardized.

Compliance with Governmental Requirements. Grantor shall comply promptly with all laws, ordinances, rules and regulations of all governmental authorities, now or hereafter in effect, applicable to the ownership, production, disposition, or use of the Collateral, including all laws or regulations relating to the undue erosion of highly-erodible land or relating to the conversion of wetlands for the production of an agricultural product or commodity. Grantor may contest in good faith any such law, ordinance or regulation and withhold compliance during any proceeding, including appropriate appeals, so long as Lender's interest in the Collateral, in Lender's opinion, is not jeopardized.

Hazardous Substances. Grantor represents and warrants that the Collateral never has been, and never will be so long as this Agreement remains a lien on the Collateral, used in violation of any Environmental Laws or for the generation, manufacture, storage, transportation, treatment, disposal, release or threatened release of any Hazardous Substance. The representations and warranties contained herein are based on Grantor's due diligence in investigating the Collateral for Hazardous Substances. Grantor hereby (1) releases and waives any future claims against Lender for indemnity or contribution in the event Grantor becomes liable for cleanup or other costs under any Environmental Laws, and (2) agrees to indemnify, defend, and hold harmless Lender against any and all claims and losses resulting from a breach of this provision of this Agreement. This obligation to indemnify and defend shall survive the payment of the Indebtedness and the satisfaction of this Agreement.

Maintenance of Casualty Insurance. Grantor shall procure and maintain all risks insurance, including without limitation fire, theft and liability coverage together with such other insurance as Lender may require with respect to the Collateral, in form, amounts, coverages and basis reasonably acceptable to Lender and issued by a company or companies reasonably acceptable to Lender. Grantor, upon request of Lender, will deliver to Lender from time to time the policies or certificates of insurance in form satisfactory to Lender, including stipulations that coverages will not be cancelled or diminished without at least ten (10) days' prior written notice to Lender and not including any disclaimer of the insurer's liability for failure to give such a notice. Each insurance policy also shall include an endorsement providing that coverage in favor of Lender will not be impaired in any way by any act, omission or default of Grantor or any other person. In connection with all policies covering assets in which Lender holds or is offered a security interest, Grantor will provide Lender with such loss payable or other endorsements as Lender may require. If Grantor at any time fails to obtain or maintain any insurance as required under this Agreement, Lender may (but shall not be obligated to) obtain such insurance as Lender deems appropriate, including if Lender so chooses "single interest insurance," which will cover only Lender's interest in the Collateral.

Application of Insurance Proceeds. Grantor shall promptly notify Lender of any loss or damage to the Collateral, whether or not such casualty or loss is covered by insurance. Lender may make proof of loss if Grantor fails to do so within fifteen (15) days of the casualty. All proceeds of any insurance on the Collateral, including accrued proceeds thereon, shall be held by Lender as part of the Collateral. If Lender consents to repair or replacement of the damaged or destroyed Collateral, Lender shall, upon satisfactory proof of expenditure, pay or reimburse Grantor from the proceeds for the reasonable cost of repair or restoration. If Lender does not consent to repair or replacement of the Collateral, Lender shall retain a sufficient amount of the proceeds to pay all of the Indebtedness, and shall pay the balance to Grantor. Any proceeds which have not been disbursed within six (6) months after their receipt and which Grantor has not committed to the repair or restoration of the Collateral shall be used to prepay the Indebtedness.

Insurance Reserves. Lender may require Grantor to maintain with Lender reserves for payment of insurance premiums, which reserves shall be created by monthly payments from Grantor of a sum estimated by Lender to be sufficient to produce, at least fifteen (15) days before the premium due date, amounts at least equal to the insurance premiums to be paid. If fifteen (15) days before payment is due, the reserve funds are

COMMERCIAL SECURITY AGREEMENT (Continued)

insufficient, Grantor shall upon demand pay any deficiency to Lender. The reserve funds shall be held by Lender as a general deposit and shall constitute a non-interest-bearing account which Lender may satisfy by payment of the insurance premiums required to be paid by Grantor as they become due. Lender does not hold the reserve funds in trust for Grantor, and Lender is not the agent of Grantor for payment of the insurance premiums required to be paid by Grantor. The responsibility for the payment of premiums shall remain Grantor's sole responsibility.

Insurance Reports. Grantor, upon request of Lender, shall furnish to Lender reports on each existing policy of insurance showing such information as Lender may reasonably request including the following: (1) the name of the insurer; (2) the risks insured; (3) the amount of the policy; (4) the property insured; (5) the then current value on the basis of which insurance has been obtained and the manner of determining that value; and (6) the expiration date of the policy. In addition, Grantor shall upon request by Lender (however not more often than annually) have an independent appraiser satisfactory to Lender determine, as applicable, the cash value or replacement cost of the Collateral.

Financing Statements. Grantor authorizes Lender to file a UCC financing statement, or alternatively, a copy of this Agreement to perfect Lender's security interest. At Lender's request, Grantor additionally agrees to sign all other documents that are necessary to perfect, protect, and continue Lender's security interest in the Property. Grantor will pay all filing fees, title transfer fees, and other fees and costs involved unless prohibited by law or unless Lender is required by law to pay such fees and costs. Grantor irrevocably appoints Lender to execute documents necessary to transfer title if there is a default. Lender may file a copy of this Agreement as a financing statement. If Grantor changes Grantor's name or address, or the name or address of any person granting a security interest under this Agreement changes, Grantor will promptly notify the Lender of such change.

GRANTOR'S RIGHT TO POSSESSION AND TO COLLECT ACCOUNTS. Until default and except as otherwise provided below with respect to accounts, Grantor may have possession of the tangible personal property and beneficial use of all the Collateral and may use it in any lawful manner not inconsistent with this Agreement or the Related Documents, provided that Grantor's right to possession and beneficial use shall not apply to any Collateral where possession of the Collateral by Lender is required by law to perfect Lender's security interest in such Collateral. Until otherwise notified by Lender, Grantor may collect any of the Collateral consisting of accounts. At any time and even though no Event of Default exists, Lender may exercise its rights to collect the accounts and to notify account debtors to make payments directly to Lender for application to the Indebtedness. If Lender at any time has possession of any Collateral, whether before or after an Event of Default, Lender shall be deemed to have exercised reasonable care in the custody and preservation of the Collateral if Lender takes such action for that purpose as Grantor shall request or as Lender, in Lender's sole discretion, shall deem appropriate under the circumstances, but failure to honor any request by Grantor shall not of itself be deemed to be a failure to exercise reasonable care. Lender shall not be required to take any steps necessary to preserve any rights in the Collateral against prior parties, nor to protect, preserve or maintain any security interest given to secure the Indebtedness.

LENDER'S EXPENDITURES. If any action or proceeding is commenced that would materially affect Lender's interest in the Collateral or if Grantor fails to comply with any provision of this Agreement or any Related Documents, including but not limited to Grantor's failure to discharge or pay when due any amounts Grantor is required to discharge or pay under this Agreement or any Related Documents, Lender on Grantor's behalf may (but shall not be obligated to) take any action that Lender deems appropriate, including but not limited to discharging or paying all taxes, liens, security interests, encumbrances and other claims, at any time levied or placed on the Collateral and paying all costs for insuring, maintaining and preserving the Collateral. All such expenditures incurred or paid by Lender for such purposes will then bear interest at the rate charged under the Note from the date incurred or paid by Lender to the date of repayment by Grantor. All such expenses will become a part of the Indebtedness and, at Lender's option, will (A) be payable on demand; (B) be added to the balance of the Note and be apportioned among and be payable with any installment payments to become due during either (1) the term of any applicable insurance policy; or (2) the remaining term of the Note; or (C) be treated as a balloon payment which will be due and payable at the Note's maturity. The Agreement also will secure payment of these amounts. Such right shall be in addition to all other rights and remedies to which Lender may be entitled upon Default.

DEFAULT. Each of the following shall constitute an Event of Default under this Agreement:

Payment Default. Grantor fails to make any payment when due under the Indebtedness.

Other Defaults. Grantor fails to comply with or to perform any other term, obligation, covenant or condition contained in this Agreement or in any of the Related Documents or to comply with or to perform any term, obligation, covenant or condition contained in any other agreement between Lender and Grantor.

False Statements. Any warranty, representation or statement made or furnished to Lender by Grantor or on Grantor's behalf under this Agreement or the Related Documents is false or misleading in any material respect, either now or at the time made or furnished or becomes false or misleading at any time thereafter.

Defective Collateralization. This Agreement or any of the Related Documents ceases to be in full force and effect (including failure of any collateral document to create a valid and perfected security interest or lien) at any time and for any reason.

Death or Insolvency. The death of Grantor, the insolvency of Grantor, the appointment of a receiver for any part of Grantor's property, any assignment for the benefit of creditors, any type of creditor workout, or the commencement of any proceeding under any bankruptcy or insolvency laws by or against Grantor.

Creditor or Forfeiture Proceedings. Commencement of foreclosure or forfeiture proceedings, whether by judicial proceeding, self-help, repossession or any other method, by any creditor of Grantor or by any governmental agency against any collateral securing the Indebtedness. This includes a garnishment of any of Grantor's accounts, including deposit accounts, with Lender. However, this Event of Default shall not apply if there is a good faith dispute by Grantor as to the validity or reasonableness of the claim which is the basis of the creditor or forfeiture proceeding and if Grantor gives Lender written notice of the creditor or forfeiture proceeding and deposits with Lender monies or a surety bond for the creditor or forfeiture proceeding, in an amount determined by Lender, in its sole discretion, as being an adequate reserve or bond for the dispute.

Events Affecting Guarantor. Any of the preceding events occurs with respect to any guarantor, endorser, surety, or accommodation party of any of the Indebtedness or guarantor, endorser, surety, or accommodation party dies or becomes incompetent or revokes or disputes the validity of, or liability under, any Guaranty of the Indebtedness.

Adverse Change. A material adverse change occurs in Grantor's financial condition, or Lender believes the prospect of payment or performance of the Indebtedness is impaired.

Insecurity. Lender in good faith believes itself insecure.

RIGHTS AND REMEDIES ON DEFAULT. If an Event of Default occurs under this Agreement, at any time thereafter, Lender shall have all the rights of a secured party under the California Uniform Commercial Code. In addition and without limitation, Lender may exercise any one or more of the following rights and remedies:

Accelerate Indebtedness. Lender may declare the entire Indebtedness, including any prepayment penalty which Grantor would be required to pay, immediately due and payable, without notice of any kind to Grantor.

Assemble Collateral. Lender may require Grantor to deliver to Lender all or any portion of the Collateral and any and all certificates of title and other documents relating to the Collateral. Lender may require Grantor to assemble the Collateral and make it available to Lender at a place to be

COMMERCIAL SECURITY AGREEMENT (Continued)

Page 4

designated by Lender. Lender also shall have full power to enter upon the property of Grantor to take possession of and remove the Collateral. If the Collateral contains other goods not covered by this Agreement at the time of repossession, Grantor agrees Lender may take such other goods, provided that Lender makes reasonable efforts to return them to Grantor after repossession.

Sell the Collateral. Lender shall have full power to sell, lease, transfer, or otherwise deal with the Collateral or proceeds thereof in Lender's own name or that of Grantor. Lender may sell the Collateral at public auction or private sale. Unless the Collateral threatens to decline speedily in value or is of a type customarily sold on a recognized market, Lender will give Grantor, and other persons as required by law, reasonable notice of the time and place of any public sale, or the time after which any private sale or any other disposition of the Collateral is to be made. However, no notice need be provided to any person who, after Event of Default occurs, enters into and authenticates an agreement waiving that person's right to notification of sale. The requirements of reasonable notice shall be met if such notice is given at least ten (10) days before the time of the sale or disposition. All expenses relating to the disposition of the Collateral, including without limitation the expenses of retaking, holding, insuring, preparing for sale and selling the Collateral, shall become a part of the Indebtedness secured by this Agreement and shall be payable on demand, with interest at the Note rate from date of expenditure until repaid.

Appoint Receiver. Lender shall have the right to have a receiver appointed to take possession of all or any part of the Collateral, with the power to protect and preserve the Collateral, to operate the Collateral preceding foreclosure or sale, and to collect the Rents from the Collateral and apply the proceeds, over and above the cost of the receivership, against the Indebtedness. The receiver may serve without bond if permitted by law. Lender's right to the appointment of a receiver shall exist whether or not the apparent value of the Collateral exceeds the Indebtedness by a substantial amount. Employment by Lender shall not disqualify a person from serving as a receiver.

Collect Revenues, Apply Accounts. Lender, either itself or through a receiver, may collect the payments, rents, income, and revenues from the Collateral. Lender may at any time in Lender's discretion transfer any Collateral into Lender's own name or that of Lender's nominee and receive the payments, rents, income, and revenues therefrom and hold the same as security for the Indebtedness or apply it to payment of the Indebtedness in such order of preference as Lender may determine. Insofar as the Collateral consists of accounts, general intangibles, insurance policies, instruments, chattel paper, choses in action, or similar property, Lender may demand, collect, receipt for, settle, compromise, adjust, sue for, foreclose, or realize on the Collateral as Lender may determine, whether or not Indebtedness or Collateral is then due. For these purposes, Lender may, on behalf of and in the name of Grantor, receive, open and dispose of mail addressed to Grantor; change any address to which mail and payments are to be sent; and endorse notes, checks, drafts, money orders, documents of title, instruments and items pertaining to payment, shipment, or storage of any Collateral. To facilitate collection, Lender may notify account debtors and obligors on any Collateral to make payments directly to Lender.

Obtain Deficiency. If Lender chooses to sell any or all of the Collateral, Lender may obtain a judgment against Grantor for any deficiency remaining on the Indebtedness due to Lender after application of all amounts received from the exercise of the rights provided in this Agreement. Grantor shall be liable for a deficiency even if the transaction described in this subsection is a sale of accounts or chattel paper.

Other Rights and Remedies. Lender shall have all the rights and remedies of a secured creditor under the provisions of the Uniform Commercial Code, as may be amended from time to time. In addition, Lender shall have and may exercise any or all other rights and remedies it may have available at law, in equity, or otherwise.

Election of Remedies. Except as may be prohibited by applicable law, all of Lender's rights and remedies, whether evidenced by this Agreement, the Related Documents, or by any other writing, shall be cumulative and may be exercised singularly or concurrently. Election by Lender to pursue any remedy shall not exclude pursuit of any other remedy, and an election to make expenditures or to take action to perform an obligation of Grantor under this Agreement, after Grantor's failure to perform, shall not affect Lender's right to declare a default and exercise its remedies.

MISCELLANEOUS PROVISIONS. The following miscellaneous provisions are a part of this Agreement:

Amendments. This Agreement, together with any Related Documents, constitutes the entire understanding and agreement of the parties as to the matters set forth in this Agreement. No alteration of or amendment to this Agreement shall be effective unless given in writing and signed by the party or parties sought to be charged or bound by the alteration or amendment.

Attorneys' Fees; Expenses. Grantor agrees to pay upon demand all of Lender's costs and expenses, including Lender's attorneys' fees and Lender's legal expenses, incurred in connection with the enforcement of this Agreement. Lender may hire or pay someone else to help enforce this Agreement, and Grantor shall pay the costs and expenses of such enforcement. Costs and expenses include Lender's attorneys' fees and legal expenses whether or not there is a lawsuit, including attorneys' fees and legal expenses for bankruptcy proceedings (including efforts to modify or vacate any automatic stay or injunction), appeals, and any anticipated post-judgment collection services. Grantor also shall pay all court costs and such additional fees as may be directed by the court.

Caption Headings. Caption headings in this Agreement are for convenience purposes only and are not to be used to interpret or define the provisions of this Agreement.

Governing Law. This Agreement will be governed by federal law applicable to Lender and, to the extent not preempted by federal law, the laws of the State of California without regard to its conflicts of law provisions. This Agreement has been accepted by Lender in the State of California.

Preference Payments. Any monies Lender pays because of an asserted preference claim in Grantor's bankruptcy will become a part of the Indebtedness and, at Lender's option, shall be payable by Grantor as provided in this Agreement.

No Waiver by Lender. Lender shall not be deemed to have waived any rights under this Agreement unless such waiver is given in writing and signed by Lender. No delay or omission on the part of Lender in exercising any right shall operate as a waiver of such right or any other right. A waiver by Lender of a provision of this Agreement shall not prejudice or constitute a waiver of Lender's right otherwise to demand strict compliance with that provision or any other provision of this Agreement. No prior waiver by Lender, nor any course of dealing between Lender and Grantor, shall constitute a waiver of any of Lender's rights or of any of Grantor's obligations as to any future transactions. Whenever the consent of Lender is required under this Agreement, the granting of such consent by Lender in any instance shall not constitute continuing consent to subsequent instances where such consent is required and in all cases such consent may be granted or withheld in the sole discretion of Lender.

Notices. Any notice required to be given under this Agreement shall be given in writing, and shall be effective when actually delivered, when actually received by telefacsimile (unless otherwise required by law), when deposited with a nationally recognized overnight courier, or, if mailed, when deposited in the United States mail, as first class, certified or registered mail postage prepaid, directed to the addresses shown near the beginning of this Agreement. Any party may change its address for notices under this Agreement by giving formal written notice to the other parties, specifying that the purpose of the notice is to change the party's address. For notice purposes, Grantor agrees to keep Lender informed at all times of Grantor's current address. Unless otherwise provided or required by law, if there is more than one Grantor, any notice given by Lender to any Grantor is deemed to be notice given to all Grantors.

Power of Attorney. Grantor hereby appoints Lender as Grantor's irrevocable attorney-in-fact for the purpose of executing any documents

COMMERCIAL SECURITY AGREEMENT (Continued)

necessary to perfect, amend, or to continue the security interest granted in this Agreement or to demand termination of filings of other secured parties. Lender may at any time, and without further authorization from Grantor, file a carbon, photographic or other reproduction of any financing statement or of this Agreement for use as a financing statement. Grantor will reimburse Lender for all expenses for the perfection and the continuation of the perfection of Lender's security interest in the Collateral.

Waiver of Co-Obligor's Rights. If more than one person is obligated for the Indebtedness, Grantor irrevocably waives, disclaims and relinquishes all claims against such other person which Grantor has or would otherwise have by virtue of payment of the Indebtedness or any part thereof, specifically including but not limited to all rights of indemnity, contribution or exoneration.

Severability. If a court of competent jurisdiction finds any provision of this Agreement to be illegal, invalid, or unenforceable as to any circumstance, that finding shall not make the offending provision illegal, invalid, or unenforceable as to any other circumstance. If feasible, the offending provision shall be considered modified so that it becomes legal, valid and enforceable. If the offending provision cannot be so modified, it shall be considered deleted from this Agreement. Unless otherwise required by law, the illegality, invalidity, or unenforceability of any provision of this Agreement shall not affect the legality, validity or enforceability of any other provision of this Agreement.

Successors and Assigns. Subject to any limitations stated in this Agreement on transfer of Grantor's interest, this Agreement shall be binding upon and inure to the benefit of the parties, their successors and assigns. If ownership of the Collateral becomes vested in a person other than Grantor, Lender, without notice to Grantor, may deal with Grantor's successors with reference to this Agreement and the Indebtedness by way of forbearance or extension without releasing Grantor from the obligations of this Agreement or liability under the Indebtedness.

Survival of Representations and Warranties. All representations, warranties, and agreements made by Grantor in this Agreement shall survive the execution and delivery of this Agreement, shall be continuing in nature, and shall remain in full force and effect until such time as Grantor's Indebtedness shall be paid in full.

Time is of the Essence. Time is of the essence in the performance of this Agreement.

Waive Jury. To the extent permitted by applicable law, all parties to this Agreement hereby waive the right to any jury trial in any action, proceeding, or counterclaim brought by any party against any other party.

DEFINITIONS. The following capitalized words and terms shall have the following meanings when used in this Agreement. Unless specifically stated to the contrary, all references to dollar amounts shall mean amounts in lawful money of the United States of America. Words and terms used in the singular shall include the plural, and the plural shall include the singular, as the context may require. Words and terms not otherwise defined in this Agreement shall have the meanings attributed to such terms in the Uniform Commercial Code:

Agreement. The word "Agreement" means this Commercial Security Agreement, as this Commercial Security Agreement may be amended or modified from time to time, together with all exhibits and schedules attached to this Commercial Security Agreement from time to time.

Borrower. The word "Borrower" means Joe Borrower and includes all co-signers and co-makers signing the Note and all their successors and assigns.

Collateral. The word "Collateral" means all of Grantor's right, title and interest in and to all the Collateral as described in the Collateral Description section of this Agreement.

Default. The word "Default" means the Default set forth in this Agreement in the section titled "Default".

Environmental Laws. The words "Environmental Laws" mean any and all state, federal and local statutes, regulations and ordinances relating to the protection of human health or the environment, including without limitation the Comprehensive Environmental Response, Compensation, and Liability Act of 1980, as amended, 42 U.S.C. Section 9601, et seq. ("CERCLA"), the Superfund Amendments and Reauthorization Act of 1986, Pub. L. No. 99-499 ("SARA"), the Hazardous Materials Transportation Act, 49 U.S.C. Section 1801, et seq., the Resource Conservation and Recovery Act, 42 U.S.C. Section 6901, et seq., Chapters 6.5 through 7.7 of Division 20 of the California Health and Safety Code, Section 25100, et seq., or other applicable state or federal laws, rules, or regulations adopted pursuant thereto.

Event of Default. The words "Event of Default" mean any of the events of default set forth in this Agreement in the default section of this Agreement.

Grantor. The word "Grantor" means Joe Borrower.

Guaranty. The word "Guaranty" means the guaranty from guarantor, endorser, surety, or accommodation party to Lender, including without limitation a guaranty of all or part of the Note.

Hazardous Substances. The words "Hazardous Substances" mean materials that, because of their quantity, concentration or physical, chemical or infectious characteristics, may cause or pose a present or potential hazard to human health or the environment when improperly used, treated, stored, disposed of, generated, manufactured, transported or otherwise handled. The words "Hazardous Substances" are used in their very broadest sense and include without limitation any and all hazardous or toxic substances, materials or waste as defined by or listed under the Environmental Laws. The term "Hazardous Substances" also includes, without limitation, petroleum and petroleum by-products or any fraction thereof and asbestos.

Indebtedness. The word "Indebtedness" means the indebtedness evidenced by the Note or Related Documents, including all principal and interest together with all other indebtedness and costs and expenses for which Grantor is responsible under this Agreement or under any of the Related Documents.

Lender. The word "Lender" means San Joaquin County Revolving Loan Fund, its successors and assigns.

Note. The word "Note" means the Note executed by Joe Borrower in the principal amount of \$50,000.00 dated September 8, 2006, together with all renewals of, extensions of, modifications of, refinancings of, consolidations of, and substitutions for the note or credit agreement.

Property. The word "Property" means all of Grantor's right, title and interest in and to all the Property as described in the "Collateral Description" section of this Agreement.

Related Documents. The words "Related Documents" mean all promissory notes, credit agreements, loan agreements, environmental agreements, security agreements, mortgages, deeds of trust, security deeds, collateral mortgages, and all other instruments, agreements and documents, whether now or hereafter existing, executed in connection with the Indebtedness.

GRANTOR HAS READ AND UNDERSTOOD ALL THE PROVISIONS OF THIS COMMERCIAL SECURITY AGREEMENT AND AGREES TO ITS TERMS. THIS AGREEMENT IS DATED SEPTEMBER 8, 2006.

COMMERCIAL SECURITY AGREEMENT
(Continued)

Page 6

GRANTOR:

X
Joe Borrower

PROMISSORY NOTE

Principal	Loan Date	Maturity	Loan No	Call / Coll	Account	Officer	Initials
\$50,000.00	09-08-2006	09-08-2011					

References in the shaded area are for Lender's use only and do not limit the applicability of this document to any particular loan or item. Any item above containing "*****" has been omitted due to text length limitations.

Borrower: Joe Borrower
123 Your Street
Stockton, CA 95201

Lender: San Joaquin County Revolving Loan Fund
56 S. Lincoln Street
Stockton, CA 95203

Principal Amount: \$50,000.00

Date of Note: September 8, 2006

PROMISE TO PAY. Joe Borrower ("Borrower") promises to pay to San Joaquin County Revolving Loan Fund ("Lender"), or order, in lawful money of the United States of America, the principal amount of Fifty Thousand & 00/100 Dollars (\$50,000.00), together with interest at the rate of 8.000% per annum on the unpaid principal balance from September 8, 2006, until paid in full. The interest rate may change under the terms and conditions of the "INTEREST AFTER DEFAULT" section.

PAYMENT. Borrower will pay this loan in 60 payments of \$1,013.82 each payment. Borrower's first payment is due October 8, 2006, and all subsequent payments are due on the same day of each month after that. Borrower's final payment will be due on September 8, 2011, and will be for all principal and all accrued interest not yet paid. Payments include principal and interest. Unless otherwise agreed or required by applicable law, payments will be applied first to any accrued unpaid interest; then to principal; then to any unpaid collection costs; and then to any late charges. Interest on this Note is computed on a 30/360 simple interest basis; that is, with the exception of odd days in the first payment period, monthly interest is calculated by applying the ratio of the annual interest rate over a year of 360 days, multiplied by the outstanding principal balance, multiplied by a month of 30 days. Interest for the odd days is calculated on the basis of the actual days to the next full month and a 360-day year. Borrower will pay Lender at Lender's address shown above or at such other place as Lender may designate in writing.

PREPAYMENT; MINIMUM INTEREST CHARGE. In any event, even upon full prepayment of this Note, Borrower understands that Lender is entitled to a minimum interest charge of \$50.00. Other than Borrower's obligation to pay any minimum interest charge, Borrower may pay without penalty all or a portion of the amount owed earlier than it is due. Early payments will not, unless agreed to by Lender in writing, relieve Borrower of Borrower's obligation to continue to make payments under the payment schedule. Rather, early payments will reduce the principal balance due and may result in Borrower's making fewer payments. Borrower agrees not to send Lender payments marked "paid in full", "without recourse", or similar language. If Borrower sends such a payment, Lender may accept it without losing any of Lender's rights under this Note, and Borrower will remain obligated to pay any further amount owed to Lender. All written communications concerning disputed amounts, including any check or other payment instrument that indicates that the payment constitutes "payment in full" of the amount owed or that is tendered with other conditions or limitations or as full satisfaction of a disputed amount must be mailed or delivered to: San Joaquin County Revolving Loan Fund, 56 S. Lincoln Street Stockton, CA 95203.

LATE CHARGE. If a payment is 15 days or more late, Borrower will be charged 6.000% of the regularly scheduled payment.

INTEREST AFTER DEFAULT. Upon default, the interest rate on this Note shall, if permitted under applicable law, immediately increase by 5.000 percentage points.

DEFAULT. Each of the following shall constitute an event of default ("Event of Default") under this Note:

Payment Default. Borrower fails to make any payment when due under this Note.

Other Defaults. Borrower fails to comply with or to perform any other term, obligation, covenant or condition contained in this Note or in any of the related documents or to comply with or to perform any term, obligation, covenant or condition contained in any other agreement between Lender and Borrower.

False Statements. Any warranty, representation or statement made or furnished to Lender by Borrower or on Borrower's behalf under this Note or the related documents is false or misleading in any material respect, either now or at the time made or furnished or becomes false or misleading at any time thereafter.

Death or Insolvency. The death of Borrower or the dissolution or termination of Borrower's existence as a going business, the insolvency of Borrower, the appointment of a receiver for any part of Borrower's property, any assignment for the benefit of creditors, any type of creditor workout, or the commencement of any proceeding under any bankruptcy or insolvency laws by or against Borrower.

Creditor or Forfeiture Proceedings. Commencement of foreclosure or forfeiture proceedings, whether by judicial proceeding, self-help, repossession or any other method, by any creditor of Borrower or by any governmental agency against any collateral securing the loan. This includes a garnishment of any of Borrower's accounts, including deposit accounts, with Lender. However, this Event of Default shall not apply if there is a good faith dispute by Borrower as to the validity or reasonableness of the claim which is the basis of the creditor or forfeiture proceeding and if Borrower gives Lender written notice of the creditor or forfeiture proceeding and deposits with Lender monies or a surety bond for the creditor or forfeiture proceeding, in an amount determined by Lender, in its sole discretion, as being an adequate reserve or bond for the dispute.

Events Affecting Guarantor. Any of the preceding events occurs with respect to any guarantor, endorser, surety, or accommodation party of any of the indebtedness or any guarantor, endorser, surety, or accommodation party dies or becomes incompetent, or revokes or disputes the validity of, or liability under, any guaranty of the indebtedness evidenced by this Note.

Adverse Change. A material adverse change occurs in Borrower's financial condition, or Lender believes the prospect of payment or performance of this Note is impaired.

Insecurity. Lender in good faith believes itself insecure.

LENDER'S RIGHTS. Upon default, Lender may declare the entire unpaid principal balance under this Note and all accrued unpaid interest immediately due, and then Borrower will pay that amount.

ATTORNEYS' FEES; EXPENSES. Lender may hire or pay someone else to help collect this Note if Borrower does not pay. Borrower will pay Lender that amount. This includes, subject to any limits under applicable law, Lender's attorneys' fees and Lender's legal expenses, whether or not there is a lawsuit, including attorneys' fees, expenses for bankruptcy proceedings (including efforts to modify or vacate any automatic stay or injunction), and appeals. Borrower also will pay any court costs, in addition to all other sums provided by law.

JURY WAIVER. To the extent permitted by applicable law, Lender and Borrower hereby waive the right to any jury trial in any action, proceeding, or counterclaim brought by either Lender or Borrower against the other.

GOVERNING LAW. This Note will be governed by federal law applicable to Lender and, to the extent not preempted by federal law, the laws of the State of California without regard to its conflicts of law provisions. This Note has been accepted by Lender in the State of California.

**PROMISSORY NOTE
(Continued)**

Page 2

COLLATERAL. Borrower acknowledges this Note is secured by the following collateral described in the security instrument listed herein: inventory, chattel paper, accounts, equipment, general intangibles and fixtures described in a Commercial Security Agreement dated September 8, 2006.

SUCCESSOR INTERESTS. The terms of this Note shall be binding upon Borrower, and upon Borrower's heirs, personal representatives, successors and assigns, and shall inure to the benefit of Lender and its successors and assigns.

NOTIFY US OF INACCURATE INFORMATION WE REPORT TO CONSUMER REPORTING AGENCIES. Please notify us if we report any inaccurate information about your account(s) to a consumer reporting agency. Your written notice describing the specific inaccuracy(ies) should be sent to us at the following address: San Joaquin County Revolving Loan Fund 56 S. Lincoln Street Stockton, CA 95203.

GENERAL PROVISIONS. If any part of this Note cannot be enforced, this fact will not affect the rest of the Note. Lender may delay or forgo enforcing any of its rights or remedies under this Note without losing them. Borrower and any other person who signs, guarantees or endorses this Note, to the extent allowed by law, waive any applicable statute of limitations, presentment, demand for payment, and notice of dishonor. Upon any change in the terms of this Note, and unless otherwise expressly stated in writing, no party who signs this Note, whether as maker, guarantor, accommodation maker or endorser, shall be released from liability. All such parties agree that Lender may renew or extend (repeatedly and for any length of time) this loan or release any party or guarantor or collateral; or impair, fail to realize upon or perfect Lender's security interest in the collateral; and take any other action deemed necessary by Lender without the consent of or notice to anyone. All such parties also agree that Lender may modify this loan without the consent of or notice to anyone other than the party with whom the modification is made. The obligations under this Note are joint and several.

PRIOR TO SIGNING THIS NOTE, BORROWER READ AND UNDERSTOOD ALL THE PROVISIONS OF THIS NOTE. BORROWER AGREES TO THE TERMS OF THE NOTE.

BORROWER ACKNOWLEDGES RECEIPT OF A COMPLETED COPY OF THIS PROMISSORY NOTE.

BORROWER:

X

Joe Borrower

AGREEMENT TO PROVIDE INSURANCE

Principal	Loan Date	Maturity	Loan No	Call / Coll	Account	Officer	Initials
\$50,000.00	09-08-2006	09-08-2011					
References in the shaded area are for Lender's use only and do not limit the applicability of this document to any particular loan or item. Any item above containing "****" has been omitted due to text length limitations.							

Grantor: Joe Borrower
123 Your Street
Stockton, CA 95201

Lender: San Joaquin County Revolving Loan Fund
56 S. Lincoln Street
Stockton, CA 95203

INSURANCE REQUIREMENTS. Grantor, Joe Borrower ("Grantor"), understands that insurance coverage is required in connection with the extending of a loan or the providing of other financial accommodations to Grantor by Lender. These requirements are set forth in the security documents for the loan. The following minimum insurance coverages must be provided on the following described collateral (the "Collateral"):

Collateral: All Inventory, Equipment and Fixtures.

Type: All risks, including fire, theft and liability.

Amount: Full Insurable Value.

Basis: Replacement value.

Endorsements: Lender loss payable clause with stipulation that coverage will not be cancelled or diminished without a minimum of thirty (30) days prior written notice to Lender.

Latest Delivery Date: By the loan closing date.

INSURANCE COMPANY. Grantor may obtain insurance from any insurance company Grantor may choose that is reasonably acceptable to Lender. Grantor understands that credit may not be denied solely because insurance was not purchased through Lender.

FAILURE TO PROVIDE INSURANCE. Grantor agrees to deliver to Lender, on the latest delivery date stated above, proof of the required insurance as provided above, with an effective date of September 8, 2006, or earlier. Grantor acknowledges and agrees that if Grantor fails to provide any required insurance or fails to continue such insurance in force, Lender may do so at Grantor's expense as provided in the applicable security document. The cost of any such insurance, at the option of Lender, shall be added to the indebtedness as provided in the security document. GRANTOR ACKNOWLEDGES THAT IF LENDER SO PURCHASES ANY SUCH INSURANCE, THE INSURANCE WILL PROVIDE LIMITED PROTECTION AGAINST PHYSICAL DAMAGE TO THE COLLATERAL, UP TO AN AMOUNT EQUAL TO THE LESSER OF (1) THE UNPAID BALANCE OF THE DEBT, EXCLUDING ANY UNEARNED FINANCE CHARGES, OR (2) THE VALUE OF THE COLLATERAL; HOWEVER, GRANTOR'S EQUITY IN THE COLLATERAL MAY NOT BE INSURED. IN ADDITION, THE INSURANCE MAY NOT PROVIDE ANY PUBLIC LIABILITY OR PROPERTY DAMAGE INDEMNIFICATION AND MAY NOT MEET THE REQUIREMENTS OF ANY FINANCIAL RESPONSIBILITY LAWS.

AUTHORIZATION. For purposes of insurance coverage on the Collateral, Grantor authorizes Lender to provide to any person (including any insurance agent or company) all information Lender deems appropriate, whether regarding the Collateral, the loan or other financial accommodations, or both.

GRANTOR ACKNOWLEDGES HAVING READ ALL THE PROVISIONS OF THIS AGREEMENT TO PROVIDE INSURANCE AND AGREES TO ITS TERMS. THIS AGREEMENT IS DATED SEPTEMBER 8, 2006.

GRANTOR:

X _____
Joe Borrower

**FOR LENDER USE ONLY
INSURANCE VERIFICATION**

DATE: _____

PHONE: _____

AGENT'S NAME: _____

AGENCY: _____

ADDRESS: _____

INSURANCE COMPANY: _____

POLICY NUMBER: _____

EFFECTIVE DATES: _____

COMMENTS: _____

DISBURSEMENT REQUEST AND AUTHORIZATION

Principal	Loan Date	Maturity	Loan No	Call / Coll	Account	Officer	Initials
\$50,000.00	09-08-2006	09-08-2011					

References in the shaded area are for Lender's use only and do not limit the applicability of this document to any particular loan or item.
Any item above containing "****" has been omitted due to text length limitations.

Borrower: Joe Borrower
123 Your Street
Stockton, CA 95201

Lender: San Joaquin County Revolving Loan Fund
56 S. Lincoln Street
Stockton, CA 95203

LOAN TYPE. This is a Fixed Rate (8.000%) Nondisclosable Loan to an Individual for \$50,000.00 due on September 8, 2011.

PRIMARY PURPOSE OF LOAN. The primary purpose of this loan is for:

☐ Personal, Family, or Household Purposes or Personal Investment.

☒ Business (Including Real Estate Investment).

DISBURSEMENT INSTRUCTIONS. Borrower understands that no loan proceeds will be disbursed until all of Lender's conditions for making the loan have been satisfied. Please disburse the loan proceeds of \$50,000.00 as follows:

Amount paid to Borrower directly: \$50,000.00
\$50,000.00 Deposited to Checking Account # 12345678

Note Principal: \$50,000.00

FINANCIAL CONDITION. BY SIGNING THIS AUTHORIZATION, BORROWER REPRESENTS AND WARRANTS TO LENDER THAT THE INFORMATION PROVIDED ABOVE IS TRUE AND CORRECT AND THAT THERE HAS BEEN NO MATERIAL ADVERSE CHANGE IN BORROWER'S FINANCIAL CONDITION AS DISCLOSED IN BORROWER'S MOST RECENT FINANCIAL STATEMENT TO LENDER. THIS AUTHORIZATION IS DATED SEPTEMBER 8, 2006.

BORROWER:

X
Joe Borrower

Exhibit "B"

COVENANTS AND CONDITIONS TO LOAN AGREEMENT

General Conditions:

- ___ 1. Borrower is to submit to RLF staff, company prepared accrual basis, semi-annual financial statements, to include balance sheet, income statement within thirty (30) days of period end.
- ___ 2. Borrower is to submit to RLF Staff, CPA accrual basis reviewed annual financial statements to include balance sheet, income statement, sources and uses of funds and reconciliation of net worth within sixty (60) days of period end.
- ___ 3. Borrower is to submit to RLF Staff, company tax returns concurrent to submission to the Internal Revenue Service.
- ___ 4. Borrower is to submit to RLF Staff, annual financial statements and tax returns of the partners within thirty (30) days of submission of tax returns to the Internal Revenue Service.
- ___ 5. The RLF must receive written notice of:
 - a.) All litigation affecting Borrower where the amount is \$5,000.00 or more;
 - b.) Any substantial dispute which may exist between Borrower and any governmental regulatory body or law enforcement authority;
 - c.) Any other matters which has resulted or might result in a material adverse change in Borrower's financial condition or operations;
- ___ 6. Borrower is not to liquidate or dissolve or enter into any consolidation, merger, pool, joint-venture, syndicate, or other combination or sell, lease or dispose of Borrower's business or assets without obtaining the RLF Board consent. The RLF Board will not unreasonable withhold consent.
- ___ 7. Borrower is to provide the RLF with personal guaranty of the managing partners.
- ___ 8. The following financial covenants are to be maintained by the Borrower throughout the loan period:
 - a.) Minimum Working Capital _____
 - b.) Minimum Current Ratio _____
 - c.) Minimum Tangible Net Worth _____
 - d.) Maximum Debt to Tangible Net Worth _____

e.) Minimum Debt Service Ratio _____

For purposes of the Loan Agreement, definitions of the above financial covenants are to be determined in accordance with generally accepted accounting principles and practices consistently applied.

- ___ 9.) Borrower shall utilize the employment services of WorkNet as a first source for hiring new personnel.
- ___ 10.) At a minimum, Borrower shall maintain and/or hire a job force at its principal place of business located in Lodi as follows:

See Exhibit "C" Attached

In the event that Borrower does not meet the hiring schedule set forth above, Borrower shall pay on a monthly basis to lender on account of principal owed by Borrower on the Note, an amount equal to two (2) times the projected employee(s) monthly salary or wage, for each employee that Borrower has failed to hire under the above schedule.

- ___ 11.) Borrower is to provide the RLF with an assignment of Keyperson Life Insurance on _____ in an amount sufficient to cover the outstanding loan balance during the life of the loan.
- ___ 12.) Owner/Partners salary/draw is not to exceed \$0 annually without prior written consent of the RLF Board. The RLF Board will not unreasonably withhold consent.
- ___ 13.) Cash or asset dividends, purchase of Treasury Stock, and loans to stockholders cumulatively are not to exceed ___% of net profit after-tax in any fiscal year, without prior written consent of the RLF Board. The RLF Board will not unreasonably withhold consent.

COLLATERAL

- ___ 14.) Borrower is to provide the RLF with purchase orders/agreement for equipment to be purchased prior to funding.
- ___ 15.) Borrower is to provide the RLF with proposed construction contract to include materials and cost breakdown prior to funding.
- ___ 16.) Borrower is to keep in force, fire, theft and hazard insurance in adequate amounts as is usual in the business carried on by the Borrower. Evidence of insurance with the RLF named as loss payee is to be provided to the RLF during the life of the loan.

**EXHIBIT E
COVENANTS & CONDITIONS**

- ___ 17a.) Borrower shall provide the RLF with a Security Agreement and UCC Filing showing the RLF in a first lien position on all new equipment purchased with RLF Loan Funds.
- ___ 17b.) Borrower shall provide the RLF with a Security Agreement and UCC filing showing the RLF in a first lien position on all equipment, now owned or hereafter acquired.
- ___ 18.) Borrower shall provide the RLF with a signed lease, acceptable to the RLF for a term not less than the term of the loan plus six (6) months and a Landlord Waiver. The Landlord Waiver to be prepared by the RLF.
- ___ 19.) Borrower shall provide the RLF with an appraisal of real property to be pledged as collateral. Appraisal shall be in form and substance as acceptable by the RLF. Cost of the appraisal to be paid by Borrower.
- ___ 20.) Title Insurance in a form acceptable to the RLF is to be obtained on all property pledged as collateral for an amount at least equal to the RLF advance against subject collateral. Cost of Title Insurance is to be paid by Borrower.
- ___ 21.) Borrower is to submit annual Employee Update to RLF Staff.
- ___ 22.) Within ninety (90) days after close of its Fiscal Year End and Annually thereafter, Borrower shall pay to the RLF, ten (10) percent of its net profits, described as net earning less partners draw. Each payment is to be applied to principal installments in the inverse order of their due dates. These payments are in addition to all other scheduled repayments and are due unless waived, in writing by the RLF Board. Waivers are to be requested in writing by Borrower sixty (60) days prior to requested payment.
- ___ 23.) Borrower is to subordinate to the RLF stockholder debt in the amount of \$0 as evidenced by the Financial Statement, for the term of the RLF loan. Interest that does not exceed market rates may be paid.
- ___ 24.) Borrower is to provide Purchase Agreement valuations of the assets in a form and substance acceptable by staff.
- ___ 25.) Lien releases are to be provided to the RLF prior to disbursements.

EXHIBIT E
COVENANTS & CONDITIONS

San Joaquin County Revolving Loan Fund

September 11, 2006

Mr. Blair King
City Manager, City of Lodi
221 W. Pine Street
Lodi, CA 95241-1910

Services provided to the City of Lodi Business Loan Program by the San Joaquin County

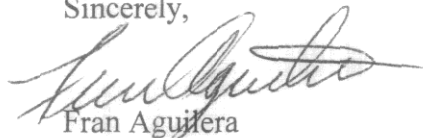
Dear Mr. King:

This letter outlines the services, which the Revolving Loan Fund may provide to the City of Lodi to support your Business Loan Program. Please note that performance of these services is subject to approval, by the San Joaquin County Board of Supervisors, of a contract for services between the Revolving Loan Fund and the City of Lodi. The RLF is capable and ready to provide any or all of the services listed below.

- Application processing
- Credit analysis/underwriting in compliance with pre-established criteria and guidelines
- Prepare credit memo describing the proposed transaction
- Present credit memo/loan proposal to loan advisory board, in conjunction with city staff
- Perform loan closing and servicing functions including payment processing, reporting, and collection of delinquent accounts
- In order to determine costs, we propose offering these services *pro bono* for the first loan.

The San Joaquin County Revolving Loan Fund (RLF) provides funding for local businesses that are unable to obtain adequate financing from traditional sources. Since inception in 1977, the RLF has lent over \$27 million to area businesses resulting in the creation of over 2,700 jobs. RLF funds were granted to the county from the federal Economic Development Administration and all loans are granted in compliance with all applicable federal regulations.

Sincerely,



Fran Aguilera
Economic Development Director

RESOLUTION NO. 2006-177

A RESOLUTION OF THE LODI CITY COUNCIL APPROVING
PROGRAM GUIDELINES OF THE REVOLVING LOAN FUND FOR
THE CITY OF LODI'S ECONOMIC DEVELOPMENT JOBS PROGRAM

=====

NOW, THEREFORE, BE IT RESOLVED that the Lodi City Council hereby approves the program guidelines (hereto attached as Exhibit A) for the Revolving Loan Program for the City of Lodi's Community Development Block Grant Economic Development Jobs Program.

Dated: September 20, 2006

=====


I hereby certify that Resolution No. 2006-177 was passed and adopted by the City Council of the City of Lodi in a regular meeting held September 20, 2006, by the following vote:

AYES: COUNCIL MEMBERS – Beckman, Hansen, Mounce,
and Mayor Hitchcock

NOES: COUNCIL MEMBERS – None

ABSENT: COUNCIL MEMBERS – Johnson

ABSTAIN: COUNCIL MEMBERS – None


JENNIFER M. PERRIN
Interim City Clerk

CITY OF LODI REVOLVING BUSINESS LOAN FUND

PROGRAM GUIDELINES

PURPOSE

The City of Lodi Revolving Loan Fund (RLF) is designed to meet the capital needs of businesses located in or moving to the City of Lodi. An RLF, in this context, refers to a loan program in which loan repayments are “revolved” or “recycled” to be loaned again in the same program

The RLF will provide appropriate assistance to businesses, which in turn create full time jobs while increasing the overall economic base of the community.

- The RLF is designed to provide no more than one-quarter of a project’s total financing requirements.
- The RLF will only provide the funds necessary to bridge the financial gap that allows the project to move forward.
- The RLF is targeted to businesses that have the greatest potential for long-term job creation, primarily benefiting persons in the Targeted Income Group¹(TIG) – which is a national objective of the HUD CDBG program. In addition, priority will be given to projects with other local public benefits, such as contribution to the City’s tax base, and local investment.

SOURCE OF FUNDING

The source of the funding for the RLF is the Community Development Block Grant Program (CDBG) of the federal Department of Housing & Urban Development (HUD) through the County of San Joaquin, and the repayment of principal and interest from existing loans. Federal requirements are incorporated into the use of these funds.

GUIDELINES AND FEATURES

There is no minimum or maximum RLF loan amount. Borrowers must, however create at least one full time equivalent job for each \$35,000, or fraction thereof, they receive in RLF assistance.

The following guidelines have been adopted to clarify the program basis for making loan commitment decisions.

- **Leveraging:** The RLF Program’s overall goal is to leverage at least three private dollars from equity and/or debt for every RLF dollar loaned. On a case-by-case basis with projects involving large job creation, this leverage requirement may be relaxed. Owner equity can be cash and/or land. Land will only be counted for construction projects. Expenditures made by the loan applicant prior to the RLF loan award are not counted unless made as part of the submittal, and made within 60 days of the application

¹ A household whose annual income is less than 80% of the county median income as defined by the County of San Joaquin CDBG Program. The income amounts change annually. See Attachment A for 2006 income levels.

submission to the RLF, and are related to and in anticipation of RLF funding. If the equity requirement is relaxed for a project, additional collateral will be required.

- **Loan Terms:** Not to exceed seven (7) years depending on the asset being financed, the financial gap, and the demonstrated need for the RLF funds. This is subject to participating lender criteria and the quality of collateral. A call provision prior to the loan maturity date may be incorporated.
- **Interest Rate:** The interest rate is set based on the business needs and financial gap of each loan. If the financial gap is the availability of capital, the interest rate shall be near market rates for the asset being financed. If the financial gap is the cost of capital (rate, term or collateral requirements), then the interest rate is set by evaluating the businesses financial condition to determine at what interest rate the proposed project and job creation become viable.
- **Loan Fees:** There is no fee charged for the Phase 1 of the loan application process, the Initial Phase. The fees for loan processing in the Second Phase range from .5 percent (.5%) to three percent (3%) of the loan amount requested, depending upon the specifics of the loan. The applicant must pay for any special services required for the loan analysis, such as title search special environmental studies, and appraisals.
- **Prepayment Penalty:** None
- **Deferral Payments:** On a case-by-case basis, payments may be deferred if warranted by the financial needs of the business.
- **Job Creation:** At least one full time equivalent job (1,750 hours annually) per \$35,000 provided (or fraction thereof) must be achieved for each business assisted. Two permanent part-time jobs (at least 875 hours annually) can be aggregated to count as one full time equivalent job in the same project. At least 51% of all jobs created/retained shall be held by Targeted Income Group (TIG) persons. See Attachment "A" for Current Income Limits of Targeted Income Group.
- **Collateral Requirements:** All RLF loans are to be fully secured for 100% collateral coverage to maintain the RLF Program. No unsecured loans shall be made. Types of collateral may include one or more of the following:
 - Real Estate – liens on real property supported by appraisals establishing sufficient equity generally utilizing a 100% loan to value ratio.
 - Deeds of Trust.
 - Liens on RLF financed machinery, equipment, or other fixtures, generally a 95% loan to value ratio.
 - Assignment of Rents, as appropriate.
 - Personal and/or Corporate Guarantees, as appropriate.
 - Cosigners and other collateral such as insurance on principals.
 - Other collateral, as appropriate.

GENERAL ADMINISTRATIVE FEATURES

- NEPA Environmental Review of business project.
- Equal Opportunity/Affirmative Action Policy.
- Attorney review of all contracts and legal forms.
- Monitoring and reporting forms.
- Collection and foreclosure policy.
- Compliance with HUD program regulations.

- Federal and State Labor Standards where applicable.

GENERAL CREDIT REQUIREMENTS

The following general credit criteria will be applied by the RLF. These requirements must be satisfied in conjunction with the provisions of RLF assistance so that the assistance is not allowed to compensate for deficiencies in these criteria. An Applicant must:

- Demonstrate the ability to operate the same type of business successfully for 3 years, or document the contracted expertise necessary to offset deficiencies in the principal's background or training.
- If circumstances warrant, agree to attend Small Business Development Center business plan, financial and marketing courses. Have enough financial strength and borrowing ability or equity to operate with the RLF assistance, on a sound financial basis.
- Show that the proposed assistance is reasonably secured to assure repayment.
- Show that the past earning record and future prospects of the business indicate ability to repay the loan and other fixed debt, if any, from the operation of the business.

ELIGIBLE APPLICANTS

Eligible applicants include on-going private, for profit business concerns, corporations, partnerships, and sole proprietorships that are classified as industrial, commercial or retail businesses, and that are located in or expanding to the City of Lodi. The project to be financed with the RLF Program must be within the incorporated area of the City of Lodi.

ELIGIBLE COSTS

- Infrastructure and off-site improvements.
- Land costs, including engineering, legal, grading, testing, site mapping and related costs associated with the acquisition and preparation of land.
- Building construction costs, including real estate, engineering, architectural, legal and related costs associated with acquisition, construction and rehabilitation of buildings and tenant improvements. (See note below regarding Labor Standards and Prevailing Wage.)
- Purchase of inventory, furniture, fixtures, machinery and equipment.
- Impact/Mitigation fees.

Special Note

The use of loan funds in private construction triggers federal Labor Standards and requires the payment of Prevailing Wage. In addition, the use of loan funds for any of the eligible costs may trigger state Prevailing Wage. This is determined on a case by case basis, and should be discussed with loan staff as early in the process as possible.

INELIGIBLE USES

- Projects which do not meet the purpose of the program are not eligible.
- Costs incurred prior to CDBG grant execution, or prior to submittal of the loan application, and prior to environmental review completion are ineligible, except for private expenditures specifically identified in the application.
- Projects, which are not located in the City of Lodi.
- Projects which involve the relocation of residents or businesses.

- Projects that propose the refinancing of existing debt are not eligible.
- Projects are not eligible if they create a conflict of interest pursuant to California Government Code Section 87100 et seq. for any current City elected official, appointed official, or employee.

OPERATION OF THE PROGRAM

The City of Lodi Business Revolving Loan Program will be operated through a combination of public and private services. The City retains the option to modify these service providers, once the program has gotten underway and the City has experience with it.

City of Lodi

- Oversight of the program
- Agreements for service with County Business RLF, and Farmers & Merchants Bank, and/or other future service providers.
- Appoints the Loan Advisory Committee.
- Marketing and initial screening of potential applicants.
- Attends Loan Advisory Committee meeting for each loan presentation.
- Annual reporting to San Joaquin County CDBG program on status of business loans, jobs created, and use of CDBG funds.
- Approval or denial of individual loans recommended by Loan Advisory Board.
- Legal review of documents
- Execution of loan documents
- Release of funds.
- Collection process
- Liaison responsibility with County CDBG program and service providers.

City's Program Operator, San Joaquin County Revolving Loan Fund

- Assist the business applicant with application process in the Second Phase of the application process.
- Conduct loan underwriting, using HUD underwriting guidelines.
- Prepare Credit Memo for Loan Advisory Committee (LAC) and present to LAC.
- Transmit the LAC action to the City Manager, with draft approval letter.
- Once loan has been made, provide loan servicing.
- Collect annual job and financial reporting from borrowers, and submit annual loan program activity report to City.
- Provide income verification process to certify Targeted Income Group benefiting from created jobs.

Farmers & Merchants Bank

- Obtain software to be used for City loan program documents.
- Prepare loan documents for each loan.
- Conduct loan closing on each loan.

LOAN APPLICATION

Initial Phase

Based upon information provided by the potential applicant, a committee of City staff will review the project for loan application appropriateness and eligibility. The Committee will be composed of the City Manager, Deputy City Manager, and Community Development Director. No fee will be charged for this phase.

Information to be provided by the potential applicant includes:

- Description of the business and project,
- Amount of loan funds requested,
- Number of jobs to be created and potential for TIG benefit
- Other public benefits
- Intended use of the funds
- Project timing and job creation timing
- Leverage and status of funding
- Environmental considerations
- Principals of the business and business plan.

Second Phase

In the event the potential project has been determined to be an eligible project and appropriate for CDBG loan consideration, the applicant will complete a Lodi Revolving Loan Fund Application.

In the Second Phase of the loan application process, the County Business Loan Program will act as the City's representative and primary contact as the loan applicant compiles all necessary loan application documents. The County Business Loan Program will conduct the loan underwriting process, using HUD Underwriting Guidelines, which are attached to these Guidelines. City staff will provide oversight to the program and all aspects of it.

As a result of the loan underwriting process, a Credit Memo will be prepared with an analysis of the loan and the recommended action to be taken. If a loan is recommended for approval, the Credit Memo will contain the loan structure, including terms and conditions. The Credit Memo will be sent to the Loan Advisory Committee.

LOAN REVIEW

The Loan Advisory Committee (LAC) is responsible for reviewing loan applications as forwarded through the Credit Memo provided by the City's Program Operator, the County RLF Program. The recommendations of the Loan Advisory Committee are made in writing to the City Manager. The City Manager will make the final decision on approval or denial of all loan applications submitted, including terms and conditions of loan agreements. All projects moving forward from the Initial Screening Phase and completed Loan Applications will be brought before the LAC.

The Loan Advisory Committee shall be composed of 3-5 persons and appointed by the City Manager. The appointments will be persons with business and/or banking experience.

On average, the RLF review process takes six to eight weeks from submittal of a complete loan application through Loan Advisory Committee review. Every effort will be made to facilitate the process to coincide with the other funding sources and the project's requirements.

LOAN CLOSING

Once the loan is approved, final loan documents will be prepared by the Farmers & Merchants Bank. The bank, acting as the city's representative, will conduct the loan closing, with oversight by City staff.

LINKING JOBS WITH TARGETED INCOME GROUP PERSONS

To assist with the job creation to benefit Targeted Income Group persons, the business will be required to sign a First Source Hiring Agreement, which commits the borrower to use the services of WorkNet, the San Joaquin County job training program, as the first source from which to hire new employees. WorkNet is accustomed to assisting employers to find workers within its clientele, and has an office in Lodi. Referrals from WorkNet will have undergone the income verification process which documents their Targeted Income Group status.

In the event the business does not hire from Worknet, the City's Program Operator, the County Business RLF, will conduct the income verification of job applicants. At least 51% of the jobs created as a result of the loan funds must be filled by persons from the Targeted Income Group.

IF JOBS NOT CREATED

In the event the business does not create the jobs as specified in the Loan Agreement and related documents, the City will declare the loan in default and require full repayment.

HOW TO GET STARTED

Please take time to read and understand the information outlined above. If you are interested in learning more about the program, please contact:

Joseph Wood
Community Improvement Manager
City of Lodi
221 West Pine Street, P. O. Box 3006
Lodi, California 95241-1910
Phone: (209) 333-6823
jwood@lodi.gov

ATTACHMENT A
CURRENT TARGET INCOME GROUP INCOME LEVELS

Family Size	Percent of Median Income			
	Very-Low		51-60%	Low
	0-30%	31-50%		
1	11,986	19,977	23,972	31,963
2	13,709	22,848	27,417	36,556
3	15,431	25,719	30,862	41,150
4	17,130	28,550	34,260	45,680
5	18,499	30,831	36,997	49,330
6	19,890	33,151	39,781	53,041
7	21,259	35,432	42,518	56,691
8	22,628	37,713	45,256	60,341
9	23,965	39,941	47,930	63,906
10	25,352	42,254	50,705	67,606
11	26,723	44,538	53,446	71,261
12	28,093	46,822	56,186	74,915
13	29,464	49,106	58,927	78,570

Note: These figures change annually, and are provided by the San Joaquin County CDBG Program.

ATTACHMENT B

LOAN UNDERWRITING GUIDELINES

The loan underwriting policies of the City of Lodi RLF are designed to assist businesses that could not proceed without the RLF assistance and to ensure that the RLF assistance is "appropriate" as defined by HUD.

HUD UNDERWRITING GUIDELINES

The City of Lodi has adopted the HUD underwriting guidelines to determine whether a proposed RLF subsidy is *appropriate* to assist the business expansion or retention. In addition, the project will be reviewed to determine that a minimum level of *public benefit* will be obtained from the expenditure of the CDBG funds.

The objectives of the underwriting guidelines are to ensure that:

Project costs are reasonable.

All sources of project financing are committed.

RLF funds are not substituted for non-Federal financial support.

The project is financially feasible.

The return on the owner's equity investment will not be unreasonably high.

RLF funds are disbursed on a pro rata basis with other financing provided to the project.

Sufficient public benefit will be received from the expenditure of RLF funds.

Project Costs: All project costs will be reviewed for reasonableness, and to avoid providing either too much or too little RLF assistance. The amount of time and resources expended evaluating the reasonableness of a cost element shall be commensurate with its costs. In some instances, it will be necessary to obtain third-party fair-market price quotations or a cost estimate. Particular attention will be focused on documenting the cost elements in a non-arm's length transaction.

Commitment of All Sources of Project Financing: Prior to the commitment of RLF funds to the project, a review shall be conducted to determine if sufficient sources of funds have been identified and committed to the project, the Borrower and participating lenders have the financial capacity to provide the funds, and to ascertain if the project is viable and will move ahead in a timely manner. In certain circumstances, the RLF may commit its funds in advance of final commitments from other funding sources. However, to conduct the underwriting analysis, the approximate terms and conditions of the other funding sources should be known. Final commitments from the other funding sources will be required, with substantially similar terms and conditions as used in the underlying analysis, prior to any loan closing or disbursement of funds.

Avoid Substitution of RLF Funds for Non-RLF Financial Support: The project will be reviewed to ensure that, to the extent practicable, RLF funds will not be used to substantially reduce the amount of non-RLF financial support for the project.

In order to receive RLF funds, a project must have a "financial gap." This gap must be documented. There are three types of financial gaps, two are discussed below, and the third is discussed under the criterion "Return on Equity Investment." One project may have two different gaps. The types of gaps are as follows:

Unavailability of Capital: The project can afford the cost of financing, but is unable to obtain the funds from either debt and/or equity sources. In regard to debt, the gap may be a result of a lender's loan to value requirements or the inherent risk of the industry or project. For example, the lender will only loan 70% of the project's cost. In this case, the business may not have the cash to bridge the gap, or if the business bridges the gap, its cash flow may be so restricted as to jeopardize the business. In order to document this gap, several steps need to be undertaken. The lender needs to be contacted to determine if there is any ability to increase the size of their loan. Other lending sources, both public and private, need to be explored. This includes looking at the business owner(s) personal financial statements for potential funds, including home equity loans. Finally, in addition to looking at the business and personal financial statements and tax returns, a proforma cash flow analysis needs to be prepared and analyzed, with and without RLF funds, to demonstrate the gap. The terms and conditions of a loan under this gap analysis should be comparable to the market.

Cost of Capital: The project cannot support the interest rate, loan term and/or collateral requirements of a lender. In analyzing this gap, discussions with the lender are important to determine any flexibility in terms. A single project may not be able to support the rate, terms and collateral requirements, or may just face a single hurdle. In addition, the gap may only exist in the early years of the project. To determine the gap, business and personal financial statements and tax returns shall be analyzed. Sources of equity shall be explored. Public and private funding sources that would bridge the gap shall be evaluated. Proforma cash flow analysis shall be developed with and without the RLF funds to demonstrate the gap. Depending on the gap, the terms or rate shall be adjusted to a rate that allows the project to proceed but are not too generous. Terms can be adjusted to allow for deferrals of principal and or interest, or to allow loans to be amortized over a longer period. Interest rates can be adjusted, including increases in the rate over time as cash flow allows.

Financial Feasibility of the Project: Each project will be examined to determine the financial viability of the project, and thus the reasonable assurance that the public benefit will be realized. The current and past financial statements for both the business and individuals must be analyzed, along with tax returns and projections. The assumptions behind the projections must be critically analyzed. Income and expense costs shall be evaluated and compared historically, where applicable, and compared to industry averages (using guides such as Robert Morris Annual Financial Statements). Project costs, including both hard and soft costs, must be determined to be reasonable. Accurate project costs are vital to determining project feasibility. As part of the financial analysis, the past, current, and projected financial data shall be analyzed to determine if the job estimates are reasonable and supportable. Labor costs shall be gauged at the break-even

point. In addition, labor costs shall be checked against industry averages. Any variations shall be explained in the loan analysis.

The terms and conditions of the RLF loan must be "appropriate." In general, the interest rate shall be set at a rate where available cash flow is able to meet debt obligations, after other obligations are met, with enough cash flow remaining to operate successfully. The loan term typically is based on the asset being financed. The term should not exceed the economic life of the asset being financed. However a longer loan amortization schedule, with the loan due at the end of the economic life may be justifiable.

Each loan shall include a written explanation of the "appropriate" analysis that was undertaken, and the reason the terms and conditions of the loan were approved. Each loan decision shall also contain a certification statement by the City Manager that the loan has been reviewed according to all underwriting guidelines and regulations and that the loan is appropriate by state/federal definition.

Financial Analysis: Historical and projected financial statements will be subject to financial analysis to determine the gap, and structure the terms and conditions of the RLF loan, as discussed above, but also to determine that the project is feasible. In addition, using prudent underwriting guidelines, demonstrate that the proposed loan is of sound value and that past earnings and future prospects indicate an ability to meet debt obligations out of profit.

Information required to be submitted by the applicant will depend on the project, ownership structure and whether it is an ongoing or start-up business. In general, the information required is outlined in the RLF checklist that will be provided.

The financial analysis will be designed to evaluate the business. The analysis will include a spread of the current and past financial statements to determine trends. The proforma statements will then be compared to these statements. Key financial ratios will be analyzed. The statements and key ratios will be compared to industry averages. Key ratios that will be analyzed include:

Current Ratio: current assets/current liabilities. The ratio is a rough indication of a firm's ability to service its current obligations. A ratio of 2:1 will be considered secure.

Quick Ratio: cash and equivalents plus accounts & notes receivable/current liabilities. This ratio is a refinement of the current ratio. A ratio of 1:1 will be used to demonstrate ample liquidity.

Cash Flow Coverage: net profit and depreciation and depletion-amortization expenses/current portion of long-term debt. This ratio will be used to measure the ability to service long term debt. This ratio is a measure of a firm's ability to meet interest payments. A cash flow coverage of 1.25 times debt service shall be used as a guideline.

Debt to Worth: total liabilities/tangible net worth. This ratio is the relationship between debt and a businesses net worth. A lower ratio is an indication of greater long-term financial safety and greater flexibility to borrow. In general, a debt to worth ratio of

higher than 5:1 shall not be exceeded as an underwriting policy. There are exceptions when the industry average is high due to its capital intensive nature or when projections show the ratio lowering quickly.

Collateral Coverage: The value of collateral is compared to the amount of the loan. Typical underwriting guidelines suggest that 125% of loan balance be used. This ratio is highly dependent on the quality and security of the collateral. The Lodi RLF shall use 100% as a guideline, which shall only be lowered with specific and detailed analysis and explanation.

Break-even Analysis: The analysis of the project's ability to support the projected labor costs and additional debt service at its break-even point (BEP) will be analyzed to determine what proportion of the jobs can be supported at that BEP. This will serve as a worst case look at the business prospects for success, ability to service new debt, and meet job creation/retention obligations.

The financial and ratio analyses must be supported by the business plan. The business plan must provide a clear understanding of the project, competition, market strategy, sales estimates, management capacity and other factors.

Lastly, to ensure project feasibility, an evaluation will be conducted of the experience and capacity of the business principals to manage the business and achieve the projections.

Return on Equity Investment: The return on equity investment is the amount of cash that the investor/business owner is projected to receive in relation to their initial equity. For a sole proprietor, this equates to salary plus net income. The RLF should not provide more than a reasonable return on investment to the business owner. This will help ensure that the RLF will maximize the use of RLF funds and not unduly enrich the business owner(s)/investor(s). However care shall be taken to ensure that the rate of return will not be too low so that the business owner's motivation remains high to pursue the business with vigor.

If the project's financial returns are projected to be too low to motivate the business and/or investor to proceed with the project, the risks of the project may outweigh the returns. An inadequate rate of return adjusted for industry and locational risks, is a third method used to determine the gap appropriate to be funded with RLF funds. To analyze this gap, the projected return on investment must be compared to the return on investment on similar projects. If it is shown that a gap does exist then the RLF financing rate and terms must be set at a rate which provides a return equal to the "market rate." Real estate appraisers and lenders will be used as sources of information on "market rate" returns.

Disbursement of RLF Funds on a Pro Rata Basis: To the extent practicable, RLF funds should be disbursed on a pro rata basis with other funding sources to avoid placing RLF funds at a greater risk than other funding sources. When it is determined that it is not practicable to disburse RLF funds on a pro rata basis, other steps shall be taken to safeguard RLF funds in the event of a default.

Standards for Evaluating Public Benefit: Each project will be reviewed to determine if a minimum level of public benefit will be obtained from the expenditure of RLF funds. The minimum standards are:

- Project site within the incorporated boundaries of the City of Lodi.
 - The project must lead to the creation or retention of at least one full-time equivalent job per \$35,000 or fraction thereof of RLF funds borrowed.
 - The timing of job creation must be reasonable in relation to the receipt of RLF assistance.
-
-

Revolving Loan Fund Program Guidelines

September 20, 2006

Presented by
Community Development Department

RLF Program Development

- February 28 - Shirtsleeve Presentation
 - Introduction to CDBG-funding for Economic Development
- March 1st - Council Action
 - \$150,000 CDBG Allocation for Economic Development Jobs Program
- July 18th - Shirtsleeve Presentation
 - Use of RLF Program for Economic Development
 - How a RLF Program would work

RLF Program Elements

- CDBG funding
 - Economic Development
 - Job Creation
- Revolving Loan Format
 - 1-2 loans per year
 - Provide CDBG allocation each year
 - Build up balance of funds through program income

RLF Program Elements

- No minimum/maximum loan amount
- Job Creation criteria
 - 1 LMI job for each \$35,000
- Leverage
 - 3:1
- Loan Terms
 - 3-7 years

RLF Program Elements

- Interest Rate
 - Near Market Rate
- Collateral
 - 100%
 - No unsecured loans

RLF Program Elements

- Loan Fees
 - .5% - 3% of Loan Amount
 - Applicant pays costs for special services
 - No Prepayment penalty
 - Payment deferral an option

RLF Program Elements

■ Eligible Uses

- Infrastructure and off-site improvements.
- Land costs, including engineering, legal, and related costs.
- Impact/Mitigation fees.
- Building construction costs, and other related costs. It is important to note that the use of loan funds may trigger Prevailing Wage requirements.

RLF Program Elements

■ Ineligible Uses

- Projects which do not meet the purpose of the program are not eligible.
- Costs incurred prior to CDBG grant execution, or prior to submittal of the loan application.
- Projects, which are not located in the City of Lodi.

RLF Program Elements

■ Ineligible Uses

- Projects which involve the relocation of residents or businesses.
- Projects that propose the refinancing of existing debt are not eligible.
- Projects are not eligible if they create a conflict of interest for any current City elected official, appointed official, or employee.

Review of RLF Process

- Loan Application Review
 - In-House, Qualitative Review
 - City Manager's Office & Community Development
- Program Operator Review
 - SJ County RLF Program
 - Quantitative Review
 - Underwriting process
 - Credit Memo – Recommendation to Loan Advisory Committee

Review of RLF Process

- Loan Advisory Committee
 - Panel of 3-5 local banking & business professionals
 - Selected from a pool of professionals recommended by City Council
 - Make recommendations to City Manager
 - Set terms and conditions
- City Manager Review
 - Final decision on approval or denial
 - Including terms and conditions

Review of RLF Process

- Loan Documents & Closing
 - F&M Bank
 - Prepares loan documents
 - LaserPro
 - Conducts closing
 - City Staff & Program Operator oversight

Review of RLF Process

- Loan Servicing – Monitoring
 - Program Operator – SJ County RLF Program
 - Payment processing
 - Reporting and Monitoring
 - Eligibility and income verification for job creation requirement
 - Collection of delinquent accounts
 - Oversight by City Staff

Conclusion

- Sample documents provided
- Staff, Consultant and Program Participants
 - Carleen Bedwell, Applied Development Economics